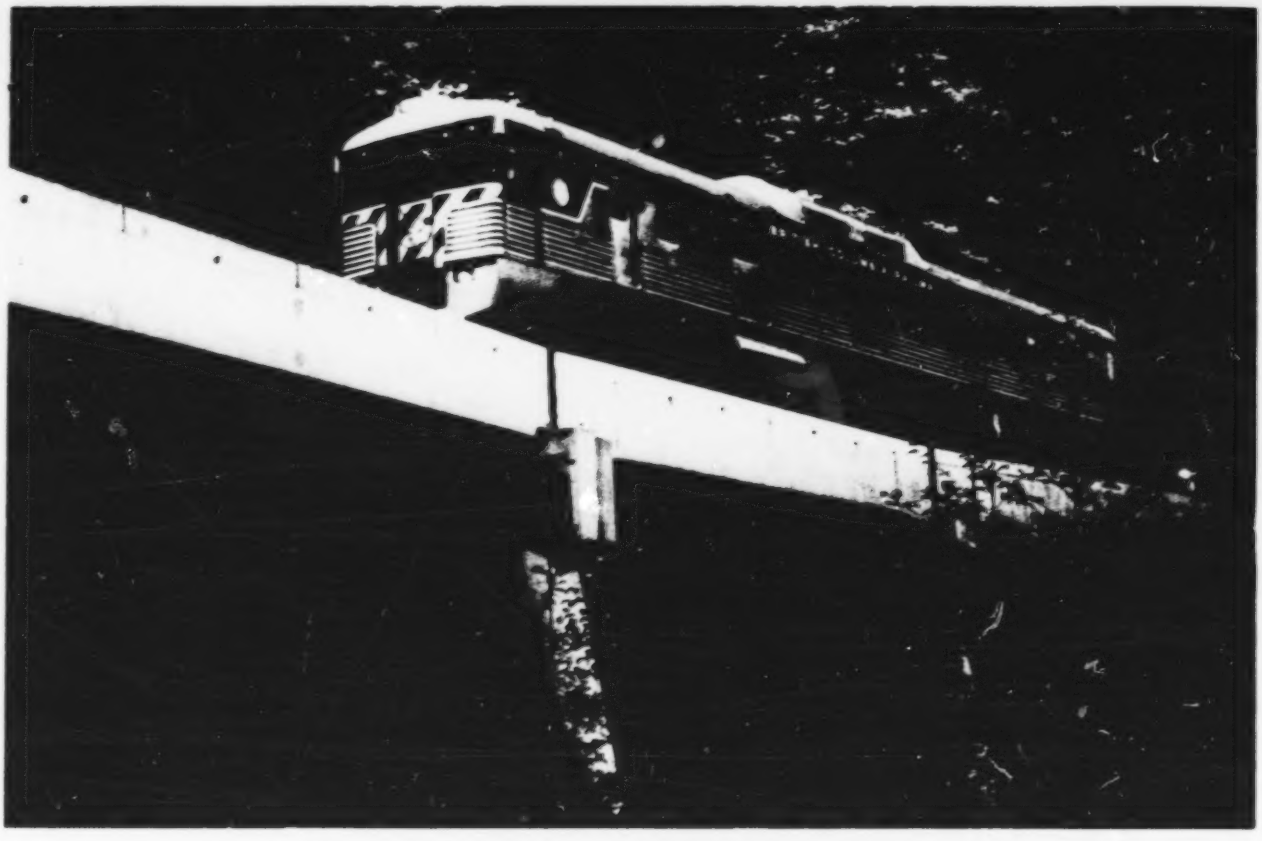
BRITISH COLUMBIA RAILWAY
1982 ANNUAL REPORT 1982



INDEX

INTRODUCTION 1 INTRODUCTION
PEOPLE 2 PEOPLE
ADMINISTRATION 4 ADMINISTRATION
INTERMODAL 5 INTERMODAL
CUSTOMER SERVICE 6 CUSTOMER SERVICE
FINANCE 8 FINANCE
COAL TRANSPORTATION 10 COAL TRANSPORTATION
MOTIVE POWER 12 MOTIVE POWER
ROLLING STOCK 14 ROLLING STOCK
MAINTENANCE 15 MAINTENANCE
LIC SYSTEM 16 LIC SYSTEM
FUTURE 17 FUTURE

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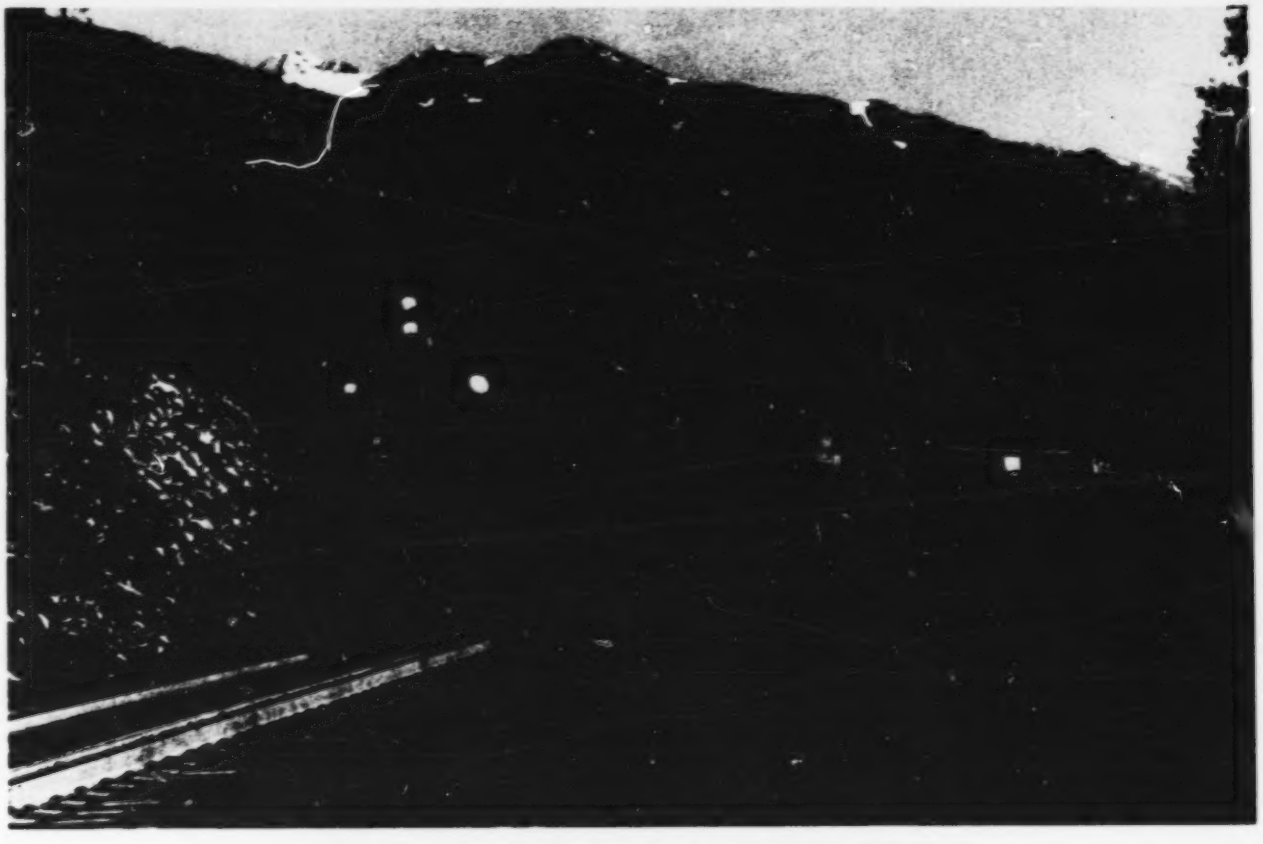


INTRODUCTION

The British Columbia Railway Company (B.C. Rail) is a commercial Crown corporation, wholly-owned by the government of British Columbia. The railway operates exclusively within provincial boundaries, with interline connections to all rail-served points in North America. While it is principally a natural resource-carrying railway, B.C. Rail also operates a limited passenger service between its home base in North Vancouver and Prince George, B.C.

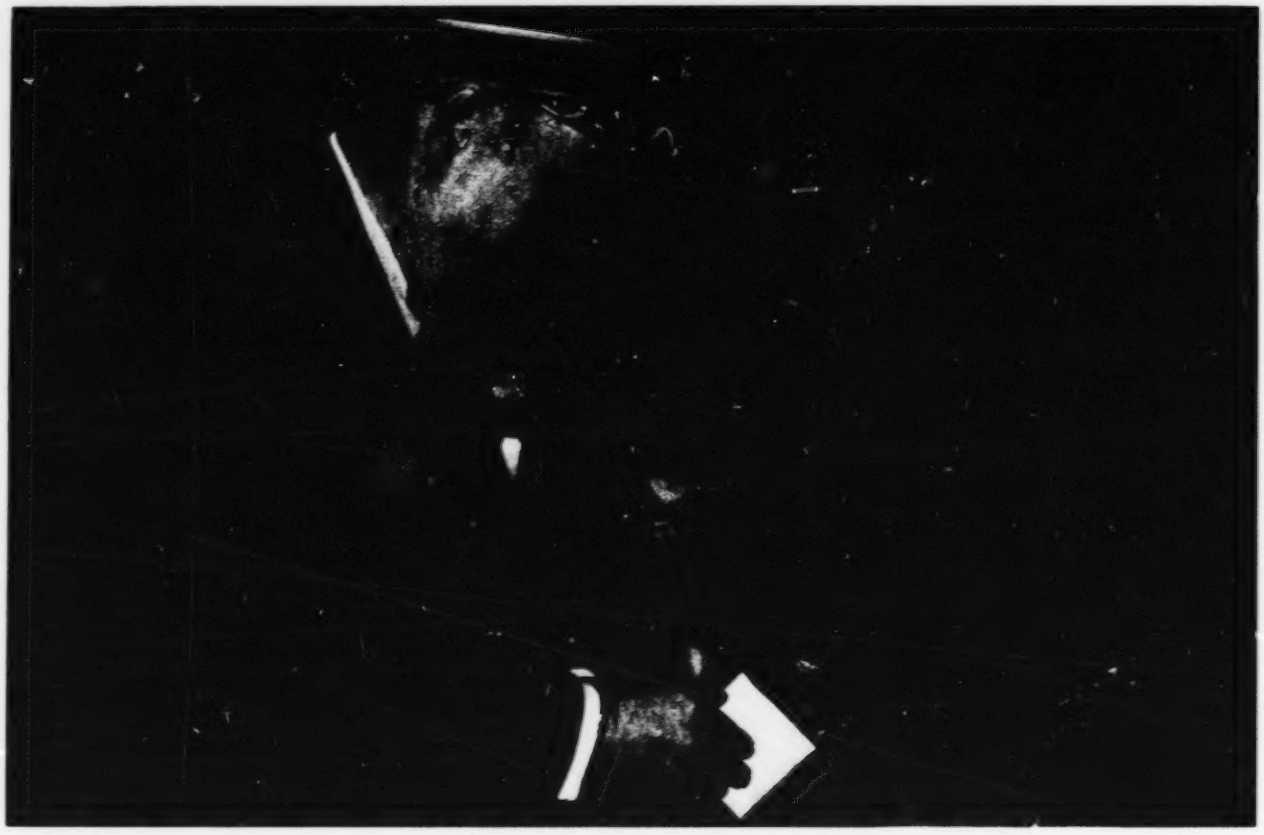
During the past 10 years, the railway has undergone an extensive rebuilding and modernization program and it is now regarded as one of the most modern and efficient rail carriers in North America. In the late 1970s, management of the company underwent a complete reorganization. An independent Board of Directors was appointed, a senior, professional railway manager became the company's first President and Chief Executive Officer and five distinct divisions were formed, each under the control of a vice-president.

Despite public ownership the railway operates in a commercial and competitive environment and it does so in expectation of profit. Responsibility for the safe, reliable and profitable operation of the company is entirely in the hands of its executive management and the government of the province no longer involves itself in the day-to-day operation of the railway.

The railway is responsive to public needs for service, where the provision of such service is economically sound. B.C. Rail encourages industrial development and has played a key role in establishing industrial parks along its trackage.

The effects of modernization on B.C. Rail's development and performance will be examined at greater length in this booklet, which is being published as a section of the company's 1982 annual report. Its purpose is to review the transformation that has taken place during the past decade and to consider some of the exciting possibilities that lie ahead.

After a troubled adolescence, B.C. Rail has come of age. It has taken its place as a leader in rail technology and operation and it faces the years ahead with confidence and optimism.



PEOPLE

At the end of 1982, B.C. Rail employed 2,400 people. While the needs, backgrounds, concerns and lifestyles of these employees differ widely, they have at least one thing in common —their employment with the railway.

Until 1981, the company's personnel and labor relations functions were separate entities. As a natural outfall of modernization, corporate reorganization, and the railway's concern for its employees, the departments were merged in 1981 to form today's Industrial Relations division.

Four departments report to the Vice-President, Industrial Relations — Compensation and Benefits; Personnel Planning; Labor Relations and Employee Services.

To be competitive in a commercial environment, the company must also compete for the highest calibre of employee. To be sure of attracting and retaining the best, a sound and properly-administered compensation program is a prerequisite. B.C. Railway's current Compensation and Benefits schedule bears comparison with any in the industry. The various programs are continuously monitored and reviewed to ensure internal and external equitability in salary and benefits administration.

The company's Personnel Planning function is responsible for the development and implementation of hiring, organizational development and training policies, as well as the computer-based Employee Information System (EIS), developed between 1980 and 1982. Since corporate reorganization began, substantial advances have been made in future needs-planning, hiring policies have been overhauled and company-wide employment standards have been established. The department's priorities for 1983 and beyond include system-wide adoption of EIS, which allows managers to retrieve departmental personnel records by computer.

By 1984, it is expected that a formal system of performance appraisal, career-path, succession and replacement planning will have been established, as well as a comprehensive inventory of employee skills.

Until 1976, the company had collective

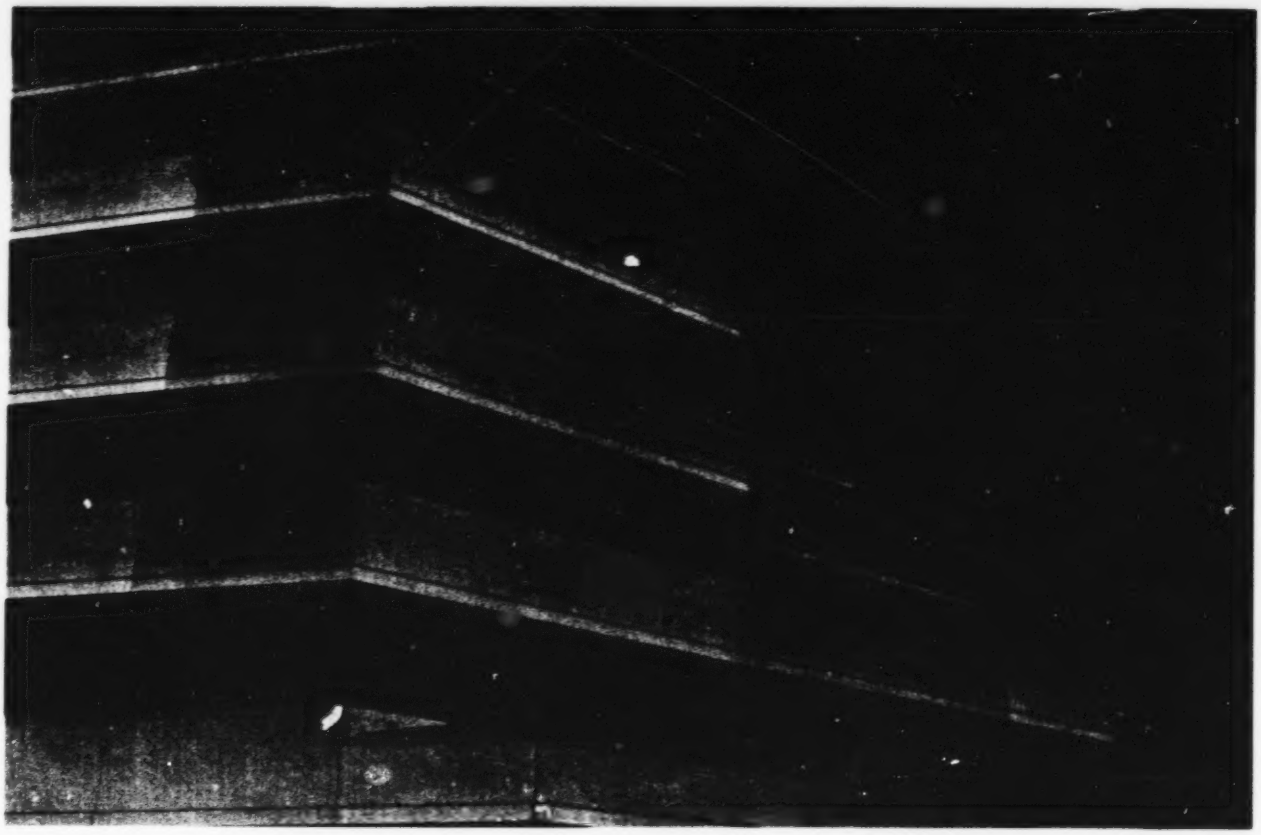
PEOPLE

agreements with each of 12 separate trade unions. That year saw the formation of the Joint Council of Trade Unions and as a direct result, the railway's relationships with its organized employees have improved substantially. A two-year collective agreement was successfully negotiated in 1981, became effective in January, 1982 and remains in force until January, 1984. While economic bargaining takes place with the joint council as a whole, trade issues bargaining continues to be the prerogative of each of the council's seven member unions. Contract administration and negotiation are the responsibility of the division's Labor Relations department.

In 1982, the company established an Employee Services department, its purpose to provide a channel of upward communication for non-organized employees. The department also has overall responsibility for the railway's Employee Assistance Program, which provides practical and professional counselling for employees suffering from the effects of drug and alcohol abuse. A full time program coordinator is assigned to this function, as well as a number of strategically-located volunteer counsellors.

The railway maintains an effective employee suggestions awards program and during 1982, first-year savings realized from the many suggestions adopted amounted to more than $70,000. The participation rate for employees is approximately 25 percent while the adoption rate for 1982 stood at 18 percent. The quality of suggestions submitted has measurably improved since the awards program was implemented and the system is regarded as an effective means of maintaining a high level of both upward and downward communication. Program objectives for future years include increased employee participation and suggestion adoption, with the emphasis on quality rather than quantity. Two major awards of $2,000 or more were made during 1982.

The railway's workforce is stable. It has a high proportion of long-service and career-minded employees and it has played a key role in the effective implementation of modernization plans during these last 10 years of progress and achievement.



ADMINISTRATION

The company's Administration division comprises six departments. The divisional Vice-President is also the railway's designated Secretary and in that capacity, responsible for legal and corporate matters.

The Real Estate and Industrial Development department manages approximately 48,000 acres (19,425 hectares) of railway property, 12,500 acres (5,060 hectares) of which are within municipal boundaries. The remainder is in the form of right-of-way, station grounds and other land holdings outside municipal boundaries. A number of sites have been developed as industrial parks, the primary objective being the development of rail freight revenues.

The railway's Communications department, which also forms part of the Administration division, provides a complete microwave communications network for railway operations. The network carries the company's internal telephone system, linking the North Vancouver head office with all points on the railway's main and branch lines.

A new streamlined Materials Management department was a natural consequence of the management reorganization of the 1970s, on the premise that expertise in this area is critical to the efficient operation of a well-run railway. Computer-assisted stores inventory management (CASIM) ensures optimum inventory levels, as well as efficient purchasing procedures. The department has acted as a role model for a number of other North American companies considering installation of similar systems.

A recent addition to the Administration division is the Office Services department, created in preparation for the company's move to its new head office, the new B.C. Rail Centre, located in North Vancouver.

The Security department is responsible for internal crime prevention and detection, the security of the railway's operation, its people, passengers and property.

The company's Public Relations department is responsible for maintaining an effective policy of open communication, both internally and externally.

INTERMODAL

B.C. Rail's Intermodal Services department was established as a profit centre, within the Marketing and Sales division, in April, 1982. It already is scoring important successes. The department markets the company's 'trailer-on-flat-car' and 'less-than-carload-lot' (LCL) services. It was formed as an answer to increasingly tough competition from the road haulage industry and already, it is proving itself competitive in price, speed and distribution efficiency.

While the railway owns and operates a wide range of road equipment, the shipment of customer-owned trailers on B.C. Rail flatcars is a growing source of revenue. The advantages to shippers include substantial reductions in trailer wear and tear, the release of customers' tractors and a greatly reduced risk of trailer damage. The railway's own fleet totals approximately 300 trailers, many of which are heated or refrigerated, and 30 tractors.

By loading trailers on B.C. Rail flatcars, for example, a Vancouver shipper with trailers destined for Prince George can avoid the time and expense of sending a tractor and driver on a long road haul but still enjoy second morning delivery service at the destination.

An advantage of Intermodal Services is its versatility in allowing tailored pickup, shipment and delivery to individual customers. From the railway's point of view, Intermodal Services generates additional traffic volume from the southern, industrialized part of the province to the north. This offers a partial correction to the imbalance between north-south traffic wherein the bulk of shipments originate in the north and are destined for markets in the south.

In a two-month period Intermodal Services moved 1,000 loads — at 50,000 pounds per load — of various construction materials over the 150 mile round trip between Chetwynd and the Tumbler Ridge construction site. Shipments, besides rail, included ties, tie plates, switches and other components of railroad building. A total of 14 tractors and 20 trailers met precise schedules to complete this massive movement of materials before road conditions deteriorated in the spring thaw.

CUSTOMER SERVICE

The economic well-being of British Columbia is inextricably linked with that of its forest industry. An estimated 50 per cent of the gross provincial product is derived from national and international sales of forest products. It follows, therefore, that a reliable and efficient transportation system is a critical element in ensuring their prompt and economical delivery to distant markets.

Competition for the carriage of B.C.'s principal commodity is intense. As well as B.C. Rail, Canada's two transcontinental carriers, the CN Rail (CNR) and CP Rail (CPR) compete for a share of market and all three railways face the growing challenge of the road transportation industry. The recession of the early 1980s created a surfeit of transportation capacity, in pursuit of a sharply-diminished source of revenue.

Since it was conceived and developed primarily as a resource-carrying system, approximately 95 per cent of B.C. Rail's freight revenue is directly or indirectly derived from the transportation of forest products. This dependency on a single traffic base will shift in 1984. But whatever the ultimate effect of northeast coal on B.C. Rail's total freight movements and revenues, the carriage of forest products will remain vital to the continued success of the company.

Aside from provincial assistance toward the cost of operating uneconomic, but socially necessary services, B.C. Rail is self-sufficient. It does not operate in a sheltered environment, protected from the realities of the market place, but competes vigorously under the same rules as other carriers.

The company's Marketing and Sales division is a product of the management reorganization that took place in 1979. Headed by a vice-president, the division embraces five departments — Sales and Service; Marketing; Pricing; Intermodal Service and Passenger Sales and Service. With few exceptions, it is a prerequisite that sales and service staff have extensive railway knowledge and, in most cases, appointments are made from within the company.

To better meet increasing competition from the road haulage industry, the division

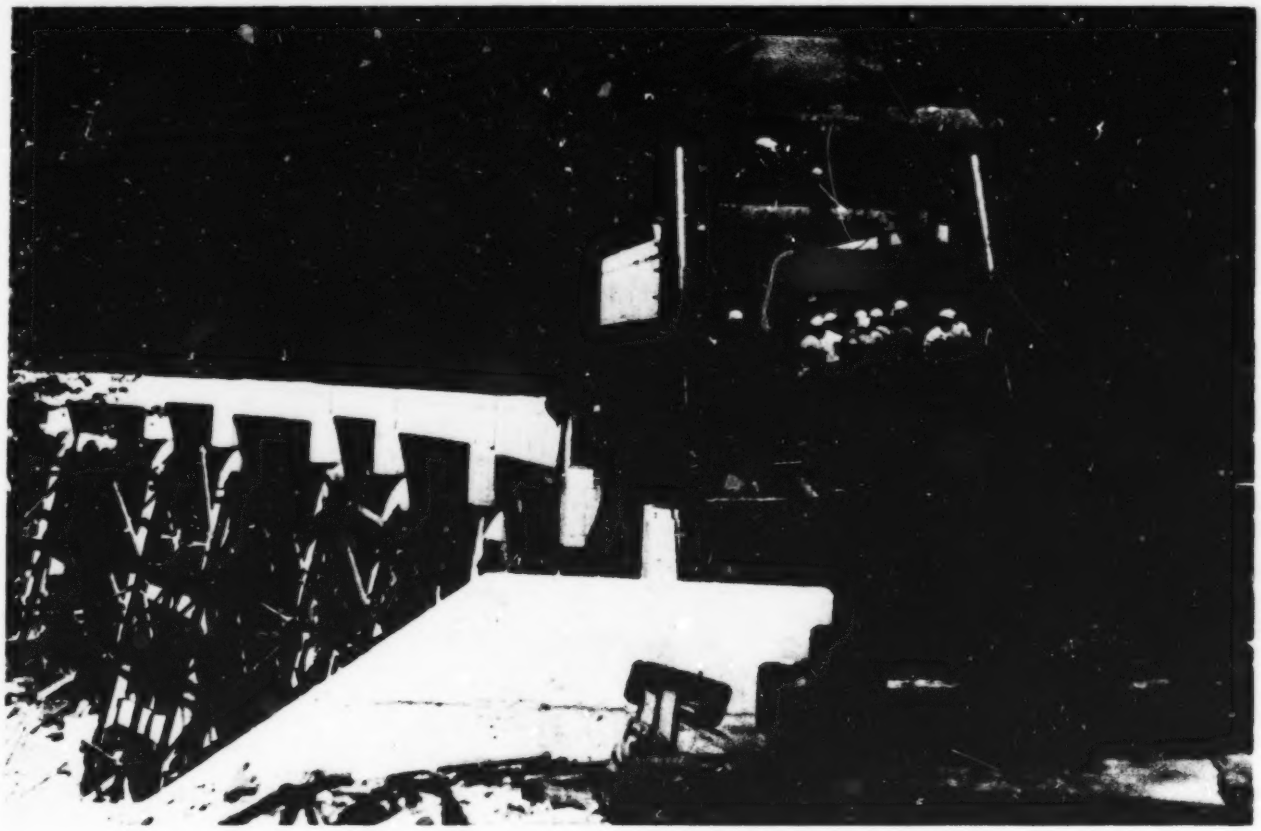
CUSTOMER SERVICE

created an Intermodal Services department in 1982. While the 'trailer-on-flat-car' (TOFC) service has been available for a number of years, it is now being aggressively marketed as an attractive alternative to conventional freight service. The product offers the economy of rail and compares with the speed of road haulage. While it is also faster than normal railcar service, it is less costly than direct road service. Its continuing development will provide increasing opportunities for the railway to develop new markets.

B.C. Rail is an originating carrier, which calls for it to own a specialized fleet of nearly 10,000 rail cars. It connects with the CN Rail at Prince George, North Vancouver and Dawson Creek, with secondary connections to CP Rail, Burlington Northern and the B.C. Hydro Railway at North Vancouver. Consequently, while it operates trains only within provincial boundaries, a large portion of B.C. Rail's originating traffic is destined to points in the United States and eastern Canada.

The Marketing and Sales division is also responsible for the railway's passenger train service, which operates between North Vancouver and Prince George. In 1982, a completely rebuilt self-propelled rail car was returned to service while the remaining cars were equipped with new engines and transmissions. The railway currently is considering ways of stimulating passenger traffic and, at the same time, improving or replacing existing equipment. It is difficult, however, to justify the substantial capital investment while demand, except during certain peak periods, remains low. By far the larger part of British Columbia's population is concentrated in the southwest corner of the province while the remaining areas served by the railway are relatively sparsely populated. The B.C. Rail mainline for the most part runs parallel with an excellent highway system and it seems unlikely that passenger demand will exceed, in the foreseeable future, the capacity the railway is already able to provide.

As of March, 1983 the Marketing and Sales division will be located in the company's new head office, the B.C. Rail Centre, at North Vancouver's Lonsdale Quay.



FINANCE

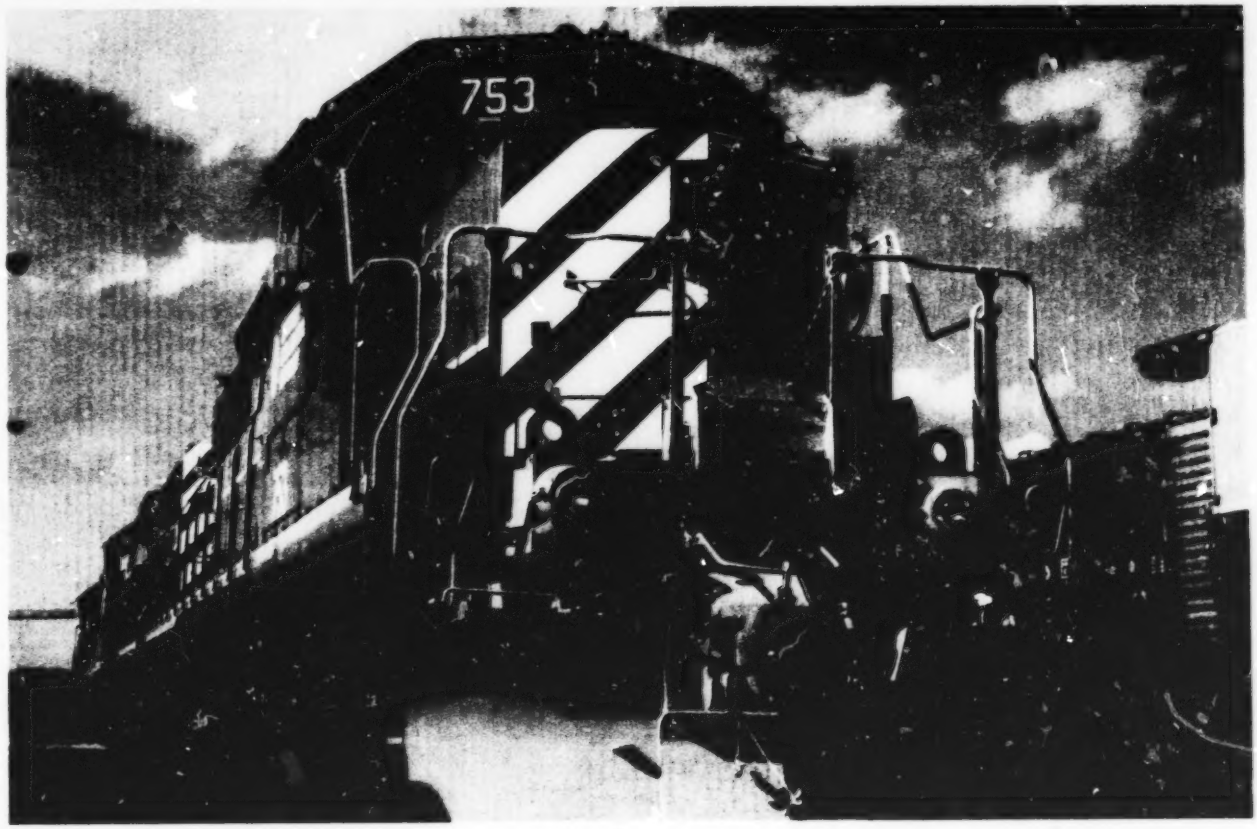
In the early 1970s, financing for expansion of the railway was obtained by the issuance of debt. By 1975, the costs of servicing this debt had reached the point where company operations no longer could support the annual debt charges.

One of the first tasks facing the company's newly-appointed board of directors was to curtail expansion and reduce uneconomic activities in order to assess whether revenues could be increased or operating costs decreased sufficiently to establish a commercially viable enterprise. Concurrently, a Royal Commission began investigating every aspect of the company's operations and, later, submitted its findings and recommendations to the provincial government.

Following the Royal Commissions's report and the submission of separate recommendations by the board of directors, the province established the practice of giving direct financial assistance to the railway. As a result, immediate charges for the servicing of historic debt, largely incurred in the early 1970s, have been financed without current additonal borrowings. Thus the company is able to retire portions of the historic debt as it becomes due and to service the interest charges and sinking fund payments on a current basis.

Simultaneously, executive management pursued the objective of limiting capital reinvestment and operating expenditures to the cash flow generated by current operations. This required new methods of financial administration and control, which were implemented and which are now performing effectively. Improvements also have been made throughout the remaining financial administrative systems in order to support the significant level of normal business activity and the additional information demands of management.

Financial arrangements for the North East Coal Development call for the railway to borrow funds directly, in order to finance new trackage construction, rolling stock manufacture and upgrading of a portion of the railway's mainline. Capital for construction of the Tumbler Ridge branch line project — which will serve the northeast coalfields —



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FINANCIAL HIGHLIGHTS

DOLLARS IN THOUSANDS

	1982	1981
Operating revenues	$ 159,696	$ 152,539
Operating expenses	$ 141,817	$ 149,483
Operating profit	$ 17,879	$ 3,056
Net income	$ 18,584	$ 3,165
Carloadings	128,577	134,982
Tons hauled	8,023,581	8,323,124
Number of employees, at year-end	2,400	2,500

OFFICERS

M.C. NORRIS, President and Chief Executive Officer
J.R. CLARKE, Vice-President — Finance
P.A. MacDONALD, Vice-President — Industrial Relations
N.A. McPHERSON, Vice-President — Operations and Maintenance
G.L. RITCHIE, Vice-President —Administration and Secretary
A.C. STURGEON, Vice-President — Marketing and Sales

BOARD OF DIRECTORS

J. NORMAN HYLAND, Chairman of the Board
J.N. FRAINE, Retired Railroader
STANLEY M. HORNER, Chartered Accountant, retired
E.C. HURD, Retired Executive
GLENN W. McPHERSON, Chairman, Vancouver Port Authority
M.C. NORRIS, President and Chief Executive Officer
HON. D.M. PHILLIPS, Minister of Industry and Small Business Development, Province of British Columbia
BRUCE ROME, Businessman
ROBERT E. SWANSON, Consulting Engineer

INDEX

F1 FINANCIAL HIGHLIGHTS
OFFICERS
BOARD OF DIRECTORS
F2 DIRECTORS' REPORT
F3 PRESIDENT'S REPORT
F5 THE YEAR IN REVIEW
F7 THE BALANCE SHEET
F8 MANAGEMENT REPORT
F9 INCOME AND DEFICIT
CHANGES IN FINANCIAL POSITION
F10 FIVE YEAR REVIEW
F11 NOTES TO FINANCIAL STATEMENTS

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DIRECTORS' REPORT

British Columbia Railway recorded a very satisfactory financial result in 1982 and the details of this operating performance are set out in the President's Report. When it is considered that this outcome was achieved in an economic environment which was far from ideal, it is particularly commendable, and the Directors congratulate the railway management and all employees for the attention to cost control and efficient operation which produced this result.

The Board's efforts and thoughts are now directed to 1983, a year which will mark two important milestones for B.C. Rail. The first of these is the completion of the Tumbler Ridge branch line and the scheduled operation of the first unit coal train in December. While this anticipation existed one and two years ago, it has now been heightened by the decision taken in 1982 to fully electrify the branch line by the utilization of 50 kilovolt technology. This will reduce the railway's dependence on hydrocarbon energy in the form of diesel fuel and place B.C. Rail in the forefront of efficient railway operation.

The second major event for the railway is the move to its new headquarters building on the Lonsdale Quay development in North Vancouver, a move which will be completed in the first quarter of 1983. The new head office structure will accommodate approximately 500 railway employees who were previously housed in nine separate locations throughout Greater Vancouver. We are confident that this centralized facility will improve inter-departmental communication and generally contribute to an efficient head office organization.

As stated in last year's annual report, the Board's policy is to build and maintain a constructive and co-operative relationship with its sole shareholder, the Province of British Columbia. In this regard, the Government of the Province has accepted the strong conviction of the Board that the cost of the Tumbler Ridge branch line, and certain additional capital costs associated with the movement of northeast coal, must be met by equity capital financing. The railway and the Province have entered into a definitive agreement with respect to this requirement, and on July 1st 1982 the Government subscribed 65 percent of the equity commitment due on that date. The next date for an equity subscription is July 1st, 1983. We have been advised, however, that while remaining committed to the principle of financing the Tumbler Ridge project with equity capital, the Province may have to defer future provisions of equity capital until provincial revenues improve. In this event, the period during which the project is financed by short term borrowing will be extended for a longer period than originally planned.

Understandably, this is a matter of major concern to the Board and to the provincial Government, but we are forced to accept its reality and hope for its early improvement and resolution.

On behalf of the Board of Directors

J.N. Hyland

J.N. Hyland
Chairman

PRESIDENT'S REPORT

Despite the generally poor state of the North American economy, I am pleased to report record net income of $18.6 million for B.C. Rail during 1982, the best performance experienced during the Company's 70-year operating history.

The results are encouraging and gratifying, and there is no doubt that 1982 is a year upon which management and employees may reflect with pride and a sense of accomplishment. Nevertheless, $18.6 million is an inadequate return on the Province of British Columbia's total investment, and falls short of what should be an attainable objective for a commercially-motivated and competitive Crown corporation such as B.C. Rail, as its traffic base increases.

As far as 1982 is concerned, the railway's earnings are largely the result of a stringent program of cost controls, first implemented during the 1981 forest industry labor dispute and vigorously applied and strengthened during the year just completed.

During this period of austerity, it was necessary to defer a number of non-essential maintenance and most developmental programs and at the same time, to reduce the railway's workforce to a level consistent with the steep decline in the economic environment. As a result of our heavy investment in rebuilding and maintenance over the past decade, it was possible to defer some of the work scheduled for 1982. In consideration of such projects, however, the safety of our employees, the general public and our operations overall, were critical factors and in this respect, no compromise was taken or contemplated. The 1982 safety performance was the best ever achieved by the railway's employees.

1982 marked the 10th anniversary of the Company's change of corporate identification, after serving the province for nearly 60 years as the Pacific Great Eastern Railway. The past decade of modernization and plant improvement contributed to the record 1982 results through increased operational efficiency.

In keeping with B.C. Rail's role as Canada's third largest railway, the physical plant is now in first class condition and it is this continuous commitment to replacement and renewal which permitted a short respite in our capital-intensive plant maintenance and improvement program. The pause, however, is a short-term measure and it is clearly recognized that the programs must soon continue, if the railway is to remain an economically healthy and efficient concern.

During the year, an average of 18 locomotives and approximately 1,416 units of rolling stock remained in storage and again, maintenance on this equipment was deferred until such time as the economy improves and they are required for service. In this case, however, monies for restoration of the equipment have been set aside, to be called upon as and when market demand improves.

The railway's decision to allow indirect, offline routing of company-owned railcars contributed significantly to 1982 revenues. As a result, other railways have been permitted to use specific car-types from the B.C. Rail fleet which in turn, provided a useful source of revenue to be offset against our own operating costs.

For the year as a whole, traffic declined by approximately 4.7 percent, largely the result of a worldwide slump in demand for B.C. lumber, the principal source of the railway's revenues. While carloadings were down, however, the effect was mitigated by a dramatic reduction in operating expenses, notwithstanding substantial increases in fuel, labor and other operating costs. Despite the difficulties of doing business during the year's depressed economic conditions, the railway's forest products business exceeded revised 1982 projections. As a result, our revenues were slightly higher than predicted in the revised forecast, but substantially lower than in the original projection compiled towards the end of 1981.

The railway's new Tumbler Ridge branch line, being built to serve British Columbia's massive northeastern coal development, is advancing on schedule and within budget. Approximately 75 percent of grade construction is complete and work on the two major tunnels has passed the 65 percent mark. First track was laid at the Anzac junction of the branch line late in 1982.

Following detailed engineering studies early in the year, it was determined that 50 kilovolt electrification of the new line was both feas-

PRESIDENT'S REPORT

ible and financially attractive and accordingly, the decision to employ this advanced technology was taken in mid-year. With excellent cooperation from both federal and provincial governments, partial funding from energy conservation sources was speedily approved and in August, seven 6,000 hp electric locomotives were ordered from General Motors' Diesel Division, in London, Ontario.

When the Tumbler Ridge branch line is completed in December, 1983, B.C. Rail will become one of only three railways in the world to use a 50 kV power supply, requiring construction of less than half the number of power sub-stations necessary for other electric railway systems.

The Company's new headquarters, under construction at the B.C. Development Corporation's Lonsdale Quay development in North Vancouver, is nearing completion and the consolidation of nine existing Greater Vancouver locations into the B.C. Rail Centre is scheduled to take place early in March, 1983. Built at a cost of approximately $15 million, the centre will be wholly-owned by the railway, with surplus space leased to tenants to help offset costs. When complete, the new centre will accommodate approximately 500 railway employees.

During the fourth quarter of 1982, rebuilding of B.C. 33 — a self-propelled combination passenger, galley and baggage car — was completed and the vehicle was returned to service in November. The work was carried out in Montreal at a cost of $1.4 million, the original intention having been to restore the entire fleet of passenger cars to an equivalent standard. The economic decline affected the availability of funds for this project, however, and along with other non-essential work, the plan was deferred. Instead, four of the remaining five Budd cars were re-engined in the Company's own shops with more powerful and efficient 340 hp Cummins motors. The sixth remains out of service following serious fire damage in mid-year.

As far as the year ahead is concerned, I am expecting no economic miracles. While there were encouraging signs towards the end of 1982 in terms of U.S. housing activity, it is clear that there is a long way to go before North America can expect to recover fully from the devastating effects of the last two years. While declining inflation and interest rates will help stimulate recovery, public confidence has been badly shaken and as a result, consumers are cautious about assuming debt.

From our own point of view, the medium-term outlook is encouraging. Our first shipments of coal begin in December, 1983 and based on existing contracts with Japanese consignees, our total annual freight movements will more than double. The immediate year ahead, however, will be a difficult one. While effective cost-controls are permanent yardsticks of good management, opportunities for cost-cutting and work deferral measures decrease in direct proportion to the frequency with which they are employed.

Consequently, opportunities to further reduce expenditures will be fewer in 1983 and inevitably, the law of diminishing returns will come into play. That, coupled with the prospect of modest economic growth in 1983, strengthens my view that there can be no room for complacency in the year ahead.

I am grateful to the managers and employees at all levels of B.C. Rail, for the consistent and loyal support they have provided in making 1982 our most successful year.

M.C. Norris

M.C. Norris
President and
Chief Executive Officer

THE YEAR IN REVIEW

The Company's 1982 operating profit was $17.9 million compared to $3.1 million for 1981. As a result of generally poor economic conditions, particularly in the British Columbia forest industry, carloadings declined by approximately 4.7 percent from 134,982 in 1981 to 128,577 in 1982.

The steep downturn in demand for B.C. forestry products was largely the result of a drastic reduction in housing starts in the United States, which normally absorbs more than 50 percent of lumber and other wood products produced in the province. When it became apparent that the B.C. forest industry would not quickly recover from the long labor dispute of 1981, the original 1982 carloading forecast was revised downwards. The 1982 results exceeded the revised forecast. However, the year's carloadings were considerably below the Company's original estimates.

Record net earnings in spite of a poor economic climate is a measure of the success of a strict program of cost controls implemented at the time of, and continued since, the 1981 forest industry closure. As a result of these controls, together with a curtailment of capital expenditures, operating expenses fell from $149.5 million in 1981 to 141.8 million in 1982, a reduction of 5 percent. No major track programs or equipment acquisitions were undertaken during the year. Because the Company's physical plant is in excellent condition, total expenditures in this area amounted to only $4.3 million, excluding the new B.C. Rail Centre.

During the year, the provincial Government purchased share capital to the value of $45 million, representing an equity contribution to the Company for costs incurred in construction of its new Tumbler Ridge line. The pace of construction on the new branch line quickened during 1982 and expenditures on this project totalled $224.7 million. In mid-year, the Company announced its decision to electrify the branch line using advanced 50 kilovolt technology. By 1984, total expenditures to construct the line, which will serve the Province's developing northeastern coalfields, will have reached $454.7 million. Funding for the project has been partially acquired through the issuance of $178.5 million in short-term notes.

The provincial Government continued to provide historic debt service assistance during the year, in addition to providing operating assistance for the passenger train service and the railway's Fort Nelson extension. These grants reflect the government's recognition of B.C. Rail's role as a vehicle for the development of northern British Columbia and as an operator of uneconomic services deemed to be in the provincial interest.

Switching revenues, that is, revenues obtained from the transfer of cars between B.C. Rail tracks and those of other carriers, were adversely affected during the year as a result of a three-week labor dispute in B.C. ports. During the period of the port shutdown, switching service was curtailed and freight service was reduced by half. A month-long construction industry dispute in the Tumbler Ridge area also had a slightly adverse impact on overall revenues but did not significantly hamper construction progress.

A total of 694 freight cars underwent major repair during the year as part of the company's continuing program of equipment maintenance. In addition, 10 diesel-electric locomotives and a Budd rail diesel car were rebuilt while 4 other Budd cars had new engine and transmission packages installed. Major repair and rebuilding activity normally would have been higher but some work was deferred as a result of the Company's restraint program. The Company's new Prince George car shop reached full production levels for the reduced staff assigned in 1982 and the shop became a significant factor in the major car repair program. Throughout the system, however, reduced staffing levels continued and as a result of reduced train service, operating and maintenance manpower was approximately 30 percent below normal.

1982 brought an encouraging improvement in the Company's safety performance, with a decline in the lost-time injury frequency rate to 30 per million man-hours from the 1981 figure of 47. The trend began in 1979 with a frequency rate of 67 per million man-hours, which declined in 1980 to 55 and has continued downward since. The 1982 performance is the best ever achieved by the railway and its employees. Accident prevention and

THE YEAR IN REVIEW

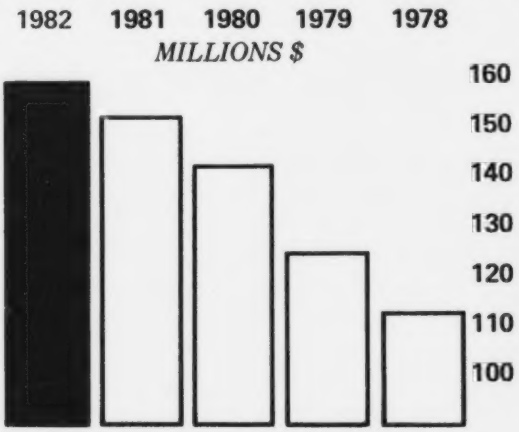
a safe working environment continue to have high priority in the Company's overall objectives.

The Company established a new Intermodal Services department in 1982, its purpose to provide a cost and time-effective alternative to conventional rail and road transportation. Intermodal Services is responsible for all 'less than carload' and 'trailer on flat car' (piggyback) activities. The department is promoting the movement of 'shipper-owned trailers,' similar to the service offered by transcontinental carriers.

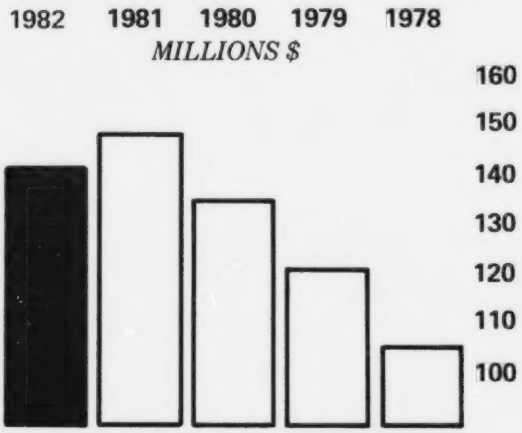
In March 1983, the Company is moving into its new head office building in North Vancouver's Lonsdale Quay development. The $15 million, six-storey building will accommodate nearly 500 employees, previously dispersed throughout nine different locations in the Vancouver area. The new building, developed by the railway, will also house retail and other commercial tenants. During 1982, real estate activities contributed approximately $3.5 million to Company revenues.

The medium to long-term outlook for B.C. Rail is encouraging. Current contracts for the shipment of northeastern coal to Japan will nearly double the Company's existing freight movements in 1984, with the prospect of substantial increases beyond. Immediate prospects for recovery in the B.C. forest industry are poor although there are indications of improvements in 1983.

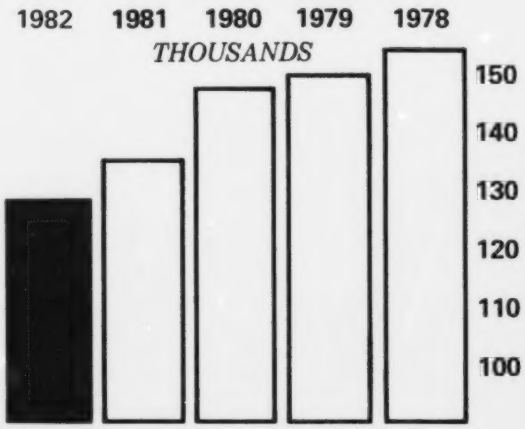
OPERATING REVENUE



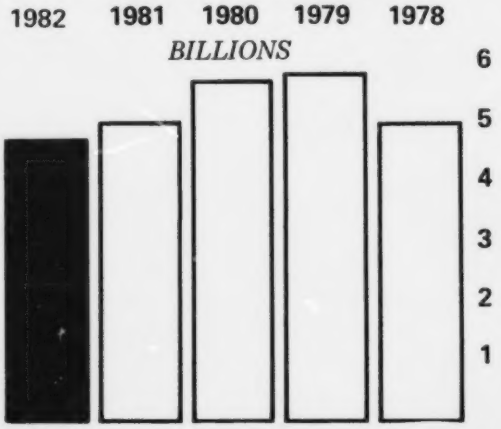
OPERATING EXPENSES



CAR LOADINGS



GROSS TON MILES



BALANCE SHEET

DOLLARS IN THOUSANDS

ASSETS	FISCAL YEAR 1982	1981
Current Assets		
Cash and temporary investments	$ 11,805	$ 7,015
Accounts receivable	31,798	22,018
Materials, supplies and other items	28,780	27,272
	72,383	56,305
Funds held in trust — Note 3	—	11,895
Property and equipment		
Road and buildings	466,219	454,924
Equipment	211,161	209,413
	677,380	664,337
Accumulated depreciation	160,457	146,359
	516,923	517,978
Tumbler Ridge branch line — Note 4	273,204	48,479
	790,127	566,457
Dease Lake Extension — Note 5	98,020	92,593
	$960,530	$727,250

On behalf of the Board:

GLENN W. McPHERSON
Director

STANLEY M. HORNER
Director

AUDITORS' REPORT

To the Lieutenant Governor in Council
Province of British Columbia

We have examined the balance sheet of British Columbia Railway Company as at December 31, 1982 and the statements of income and deficit and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these financial statements present fairly the financial position of the railway as at December 31, 1982 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Peat, Marwick, Mitchell & Co.

Chartered Accountants
Vancouver, British Columbia, Canada
February 28, 1983

BALANCE SHEET

DOLLARS IN THOUSANDS

LIABILITIES AND SHAREHOLDER'S EQUITY	FISCAL YEAR 1982	1981
Current Liabilities		
Accounts payable and other liabilities	$105,794	$ 80,651
Current obligations on long-term debt	9,456	10,935
	115,250	91,586
Notes payable — Note 4	178,517	32,000
Long-term debt — Note 6	636,444	656,944
Shareholder's equity		
Share capital — Note 7	230,573	185,573
Contributed surplus — Government grants — Note 8	113,852	93,837
	344,425	279,410
Deficit	(314,106)	(332,690)
	30,319	(53,280)
Commitments and contingent liabilities — Notes 4, 9, 10 and 11		
	$960,530	$727,250

MANAGEMENT REPORT

The financial statements of the British Columbia Railway Company have been prepared by management in accordance with accounting principles generally accepted in Canada for railways in a manner consistent with the previous year. Management is responsible for the accuracy, integrity and objectivity of the information contained in the financial statements and to ensure that the presentation conforms with generally accepted accounting principles.

The independent auditors, Peat, Marwick, Mitchell & Co., have been appointed by the Lieutenant Governor in Council to express an opinion as to whether these financial statements present fairly the railway's financial position and operating results in conformity with generally accepted accounting principles consistently applied. Their report outlines the scope of their examination and gives their opinion on the fairness of the statement presentation.

The Audit Committee of the railway directors appointed by the board meets periodically with financial officers of the railway and the external auditors to ensure that each group is fulfilling its obligations and to review and approve the annual financial statements prior to their release.

Management maintains an extensive system of internal accounting controls and believes that transactions are accurately recorded on a timely basis, are properly approved and result in reliable financial statements. The adequacy and operation of the control systems are monitored on an on-going basis by an internal audit department.

The financial statements have, in the opinion of the management of the railway, been properly prepared within reasonable limits of materiality and within the framework of the accounting policies summarized in Note 1 of the Notes to the financial statements.

INCOME AND DEFICIT

DOLLARS IN THOUSANDS

	FISCAL YEAR 1982	1981 NOTE 2
Operating revenues	$159,696	$152,539
Operating expenses		
Operations	46,883	47,266
Road maintenance	25,759	28,582
Equipment maintenance	45,281	46,146
Depreciation	17,436	17,125
Other	15,183	14,176
Government assistance — Note 12	(8,725)	(3,812)
	141,817	149,483
Railway operating profit	17,879	3,056
Other income (expense)		
Interest expense — Note 8	(52,303)	(54,800)
Application of debt servicing grant	49,985	52,591
	(2,318)	(2,209)
Other income	3,023	2,318
	705	109
Net income	18,584	3,165
Opening deficit	332,690	335,855
Closing deficit	$314,106	$332,690

CHANGES IN FINANCIAL POSITION

DOLLARS IN THOUSANDS

	FISCAL YEAR 1982	1981
Funds provided		
Operations		
Net income	$ 18,584	$ 3,165
Add depreciation	17,436	17,125
	36,020	20,290
Long term financing	153,138	43,308
Contributed surplus		
Construction	—	2,700
Debt servicing — Note 8	20,015	17,409
Share issue	45,000	—
Government grants		
Construction — Note 12	271	3,166
Passenger car modernization — Note 13	1,724	658
	256,168	87,531
Funds used		
Funds held in trust — Note 3	(11,895)	11,895
Property and equipment	243,102	72,579
Dease Lake Extension — Note 5	5,427	87
Sinking funds and long-term debt	27,120	25,575
	263,754	110,136
Working capital (deficiency)		
Increase (decrease)	(7,586)	(22,605)
Opening balance	(35,281)	(12,676)
Closing balance	$(42,867)	$(35,281)

FIVE YEAR REVIEW

DOLLARS IN THOUSANDS

	FISCAL YEAR				
	1982	**1981**	**1980**	**1979**	**1978**
STATEMENT OF INCOME					
Operating revenues	$159,696	$152,539	$143,726	$125,826	$114,309
Operating expenses					
Operations	46,883	47,266	46,510	40,979	36,226
Road maintenance	25,759	28,582	28,920	28,369	23,914
Equipment maintenance	45,281	46,146	43,567	39,192	30,731
Depreciation	17,436	17,125	14,279	13,364	13,585
Other	15,183	14,176	9,462	8,354	9,402
Government grants	(8,725)	(3,812)	(6,510)	(8,888)	(8,237)
	141,817	149,483	136,228	121,370	105,621
Railway operating profit	17,879	3,056	7,498	4,456	8,688
Other income (expense)					
Interest expense	(52,303)	(54,800)	(58,472)	(54,053)	(54,338)
Application of debt servicing grant	49,985	52,591	57,522	—	—
Net interest expense	(2,318)	(2,209)	(950)	(54,053)	(54,338)
Other income	3,023	2,318	6,094	1,462	1,202
	705	109	5,144	(52,591)	(53,136)
Net income (loss)	$18,584	$3,165	$12,642	$(48,135)	$(44,448)
OPERATING STATISTICS					
Total revenue cars loaded on line	126,031	131,624	143,609	144,398	149,597
Received from connections	2,546	3,358	4,634	5,525	5,253
Total carloadings	128,577	134,982	148,243	149,923	154,850
ROLLING STOCK FLEET					
Motive power diesel units	126	126	126	116	119
Freight cars	9,811	9,855	9,966	9,862	9,376
Passenger cars	6	6	7	8	6
Boarding and work cars	493	504	509	538	549
TONS HAULED	8,023,581	8,323,124	8,663,746	8,599,215	8,842,253
EMPLOYEES AT YEAR END	2,400	2,500	2,800	2,950	2,950

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 1982

1. SIGNIFICANT ACCOUNTING POLICIES

The accounting regulations prescribed by the Canadian Transport Commission for Canadian railways have been adopted to the extent that this is possible without submitting specific accounting policies and depreciation rates to the Commission for approval.

CLASS OF BUSINESS

The railway provides a fully integrated rail service within the Province of British Columbia. Services other than hauling freight are not of sufficient size to warrant separate reporting.

ROAD PROPERTY

New construction is recorded at cost, net of Government grants received. Abandoned or relocated sections are removed at average unit costs. Elements of track structure installed during planned programs are recorded at cost and the material released is removed at amounts which approximate the average unit cost. Labour costs for programmed replacements are expensed as incurred.

All costs of constructing extension lines are capitalized to the date the line is certified operational by the British Columbia Ministry of Transportation and Highways. Capitalization of interest ceases and provision of depreciation commences on the date of certification.

DEPRECIATION

Depreciation is provided for major categories of property and equipment on the straight-line basis at composite rates estimated to reduce the original cost to estimated salvage value over the average service lives of the classes. The group method is used for recording depreciation under which the original cost of assets retired less salvage value is charged against accumulated depreciation. No gain or loss on retirements, other than on accidental destruction of rolling stock and on disposal of land, is included in operations. The original cost of principal assets less estimated salvage value is depreciated over the following number of years: Grades, surfacing and tunnels — 100, Rails — 50, Ties — 20, Ballast — 25, Bridges — 30-80, Locomotives and power units — 25, Freight cars — 33.

REPAIRS

Repairs and non-programmed replacements of track structure are charged against current operations. Betterments and major track relocations are capitalized.

MATERIALS AND SUPPLIES

Inventories of materials and supplies are valued at the lower of average cost or net realizable value.

GOVERNMENT ASSISTANCE

Government assistance has been recorded in accordance with the accounting recommendations of the Canadian Institute of Chartered Accountants. Grants directly related to the construction or rehabilitation of road property have offset related road property capital expenditures. Operating grants have been deducted from the related expense accounts. Assistance provided by Government in its capacity as shareholder has been credited to contributed surplus.

AMORTIZATION OF BOND DISCOUNT ON SINKING FUND INVESTMENTS

During the year, bonds issued by a related Provincial Crown corporation were acquired to be held as assets in the sinking funds. These bonds were acquired at a discount of $11,575,000 in a transaction structured to yield current market interest rates for the railway's sinking funds through the amortization of the discount. It is the intention to hold these bonds to maturity therefore $616,000 has been recognized as income in the current year. All other bond discounts will be recognized at maturity.

INCOME TAXES

The railway is exempt from Canadian federal and provincial income taxes.

TRANSACTIONS IN FOREIGN CURRENCY

Transactions originating in United States currency are recorded at the approximate exchange rates prevailing at the dates of the transactions. Current assets and current liabilities have been translated to equivalent Canadian amounts at the rate of exchange in effect on the balance sheet date.

LEASES

Certain long-term lease transactions relating to the financing of equipment are accounted for as purchases of property. The capitalized lease obligation reflects the present value of future rental payments discounted at the interest rate implicit in the lease. The capitalized value of depreciable assets is depreciated over the term of the lease in equal annual amounts. The costs of all other leases are charged against operations as they are incurred.

FISCAL YEAR

The fiscal year of the railway ends on the Friday closest to December 31. The 1982 fiscal year ended on December 31, 1982 and the 1981 fiscal year ended on January 1, 1982; both comprised 52 weeks.

2. RECLASSIFICATION

The 1981 operating expenses have been reclassified to correspond to the classifications prescribed by the Canadian Transport Commission. Expenses relating to rolling stock previously shown as Operations and Road Maintenance have been classified as Equipment Maintenance in 1982.

3. FUNDS HELD IN TRUST

In 1981, a judgement was rendered by the British Columbia Supreme Court awarding two contractors costs and interest resulting from litigation concerning construction of the Dease Lake Extension. An amount of $11,895,077 was paid to the Court in trust pending resolution of the railway's appeal of this judgement. In 1982 the British Columbia Court of Appeal overturned a portion of the Lower Court ruling. The net amount of the final judgement of $5,273,000 together with legal costs of $154,000 have been capitalized as a cost of the Dease Lake Extension. The balance of funds have yet to be released from the Court and are included in accounts receivable.

4. TUMBLER RIDGE BRANCH LINE

In 1981, the railway began construction of the 130 km Tumbler Ridge branch railway line to the coal fields located in northeastern British Columbia. Since inception of this project, the Government of the Province of British Columbia has granted $2,700,000, purchased $45,000,000 share capital and arranged the railway's interim financing to construct the branch line.

The Government of the Province of British Columbia intends to retire the interim financing with equity capital financing. Until such time as the interim financing is fully retired, the Province intends to annually subscribe for equity capital equivalent to the amount of interest capitalized and to provide annual grants equivalent to the amount of interest charged to operations.

The total construction cost of the branch line, excluding capitalized financing charges, is currently projected at $455,000,000. As of December 31, 1982, the railway has awarded construction contracts of $304,000,000. The Government of the Province of British Columbia has arranged interim financing by notes due January 7, 1983 in the aggregate of $178,517,000. These notes bear interest at a rate equal to the Canadian bank prime rate less ½ percent determined monthly on the anniversary date of issuance. Subsequently, these notes were retired using the proceeds of newly issued short-term notes and acceptances. The interim financing obligations are debts of the railway which will be repaid out of monies to be provided by the Province.

5. DEASE LAKE EXTENSION

These costs consist of charges relating to the uncompleted Dease Lake Extension prior to suspension of construction in 1977 and legal and other costs incurred subsequently in connection with litigation commenced against the railway by contractors involved in construction of the extension. There are no commitments to continue construction and in the event any portion of this extension is abandoned, the cost less any value recovered will be written off at that time.

6. LONG-TERM DEBT

Long-term debt is not secured by assets of the railway. Bonds issued by the railway which are held in the sinking fund are not cancelled prior to maturity but for financial statement presentation have been deducted from the amounts shown as outstanding. As of December 31, 1982 the principal amount of bonds issued by the railway held in the sinking fund aggregated $5,320,000. (1981 — $25,378,000).

Long-term debt outstanding, less current maturities, consists of the following:

	1982 $000	1981 $000
Sinking fund bonds and debentures		
1983—1987, 3.25—5%	$ 34,204	$ 15,129
1988—1992, 5.75—7.66%	40,415	61,148
1993—1997, 4.5—9.34%	237,040	165,669
1998—2002, 7.48—10.5%	383,348	444,003
2003—2005, 12.75%	45,000	75,000
	740,007	760,949
Less sinking fund assets net of railway's own bonds held	132,249	125,161
	607,758	635,788
Notes and bonds 16.875% — due 1986 and 199¢	17,662	11,042
Serial bonds 4.875% — due 1988	1,072	1,222
Long-term lease obligations	19,408	19,827
	645,900	667,879
Deduct current portion	9,456	10,935
	$636,444	$656,944

Bonds totalling $185,327,000 which are held by the Minister of Finance for Canada contain a provision whereby under certain circumstances they may be presented for redemption upon six months notice given to the railway. A further $13,738,000

of bonds are subject to redemption in various amounts at various dates until 1984, at the option of either the holder or the railway. The railway also has the right under certain circumstances to redeem bonds aggregating $476,651,000 at various dates, principally after 1983.

Long-term debt retirements and sinking fund provisions excluding obligations under capital leases and early redemption options, for the four fiscal years ending with 1987 are $9,539,000, $9,548,000, $18,410,000 and $9,570,000.

Included in long-term debt outstanding at December 31, 1982 are obligations recorded at $28,733,000 with a par value of $26,071,000 payable in United States currency. The Canadian equivalent of these obligations at December 31, 1982 is approximately $32,052,000.

The Government of the Province of British Columbia has unconditionally guaranteed the principal and interest of the serial bonds, notes and sinking fund bonds and debentures.

7. SHARE CAPITAL

Authorized share capital is 10,000,000 shares of $100.00 each. During the year, 450,000 shares were issued for $45,000,000, increasing the number of shares outstanding to 2,305,729.

8. INTEREST EXPENSE

The Government of the Province of British Columbia has granted $70,000,000 to assist in paying the 1982 historic debt servicing charges of the railway. Of this amount, $49,985,000 has been applied to offset interest on long-term debt and the balance of $20,015,000 has been added to contributed surplus.

Interest expense is as follows:

	1982 $000	1981 $000
Interest on long-term debt and notes	$84,200	$72,803
Less:		
Sinking fund earnings	14,442	13,450
Interest capitalized	14,071	1,743
Interest earned on temporary investments	5,702	5,019
	34,215	20,212
	49,985	52,591
Interest on capitalized leases	2,318	2,209
	52,303	54,800
Less:		
Application of debt servicing grant	49,985	52,591
Net interest	$ 2,318	$ 2,209

9. LEASE COMMITMENTS

The railway has significant lease commitments for rolling stock and additional minor lease commitments for equipment and real estate which expire at various dates prior to the year 2000. Certain of these leases transfer substantially all of the benefits and risks of ownership to the railway and are accounted for as capital assets.

The following is a schedule of future minimum rental payments at December 31, 1982 required under non-cancellable leases that have terms in excess of one year:

	Capital Leases $000	Operating Leases $000
1983	$ 3,091	$13,109
1984	3,091	12,292
1985	3,091	9,860
1986	3,091	9,737
1987	3,091	9,683
Later years	31,682	44,945
Total minimum lease payments	47,137	$99,626
Less:		
Executory costs	(4,502)	
Imputed interest	(23,227)	
Present value	$19,408	

Assets under capital leases recorded in the property and equipment accounts as at December 31, 1982 are as follows:

Equipment	$20,316
Accumulated depreciation	2,662
	$17,654

10. CONTINGENT LIABILITIES

The railway is contingently liable with respect to pending litigation and claims which arise in the normal course of business. In the opinion of management any liability that may arise from such contingencies would not have a material adverse effect on the financial statements of the railway.

In connection with construction of the Tumbler Ridge branch line, certain contractors have made claims, or have indicated their intention to make claims, against the Company for construction work completed to date. In the opinion of the management, such claims, if successful, should not exceed $10 million in the aggregate. Any amounts paid by the Company will be capitalized as costs of the Tumbler Ridge branch line.

11. PENSION PLAN

The majority of the railway's employees participate in a contributory pension plan and are entitled to limited vested rights prior to retirement. Independent actuaries performed an actuarial valuation of the plan as at December 31, 1981. Based on their report, the unfunded actuarial liabilities of the plan at that date approximated $8,600,000. These unfunded liabilities are being amortized over a period of 21 years from that date at a rate of $972,000 per annum.

The total pension expense for the year, including amortization payments was $5,591,000 (1981 — $5,576,000).

12. GOVERNMENT ASSISTANCE

Total grants received from the Government of the Province of British Columbia were as follows:

	1982 $000	1981 $000
Debt servicing (Note 8)	$70,000	$70,000
Fort Nelson Extension		
Operating	5,837	3,812
Rehabilitation	271	3,166
Passenger operation		
1982	1,763	—
1981	1,125	—
Passenger car modernization	700	1,700
	$79,696	$78,678

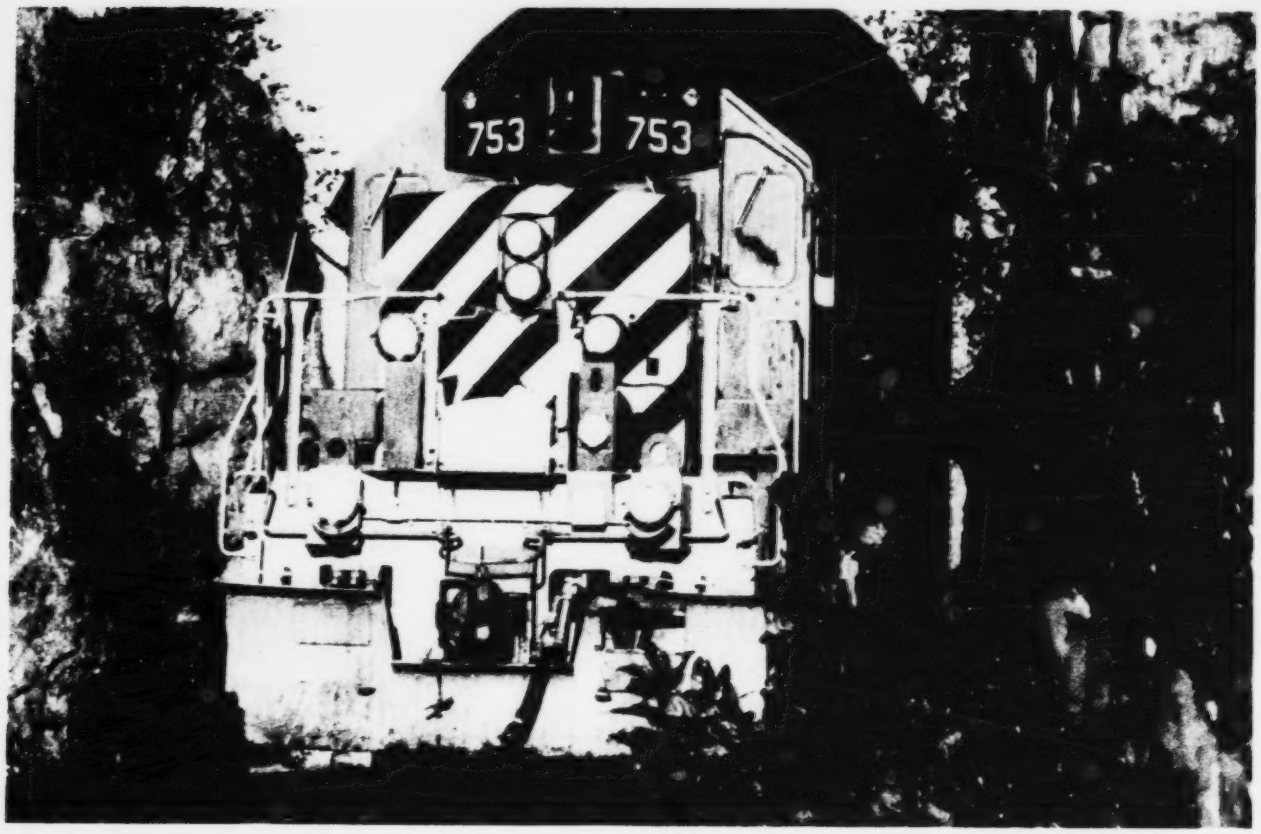
Of the above, the following were treated as a reduction in operating expenses:

Passenger operation		
1982	$1,763	—
1981	1,125	—
Fort Nelson Extension	5,837	3,812
	$8,725	$3,812

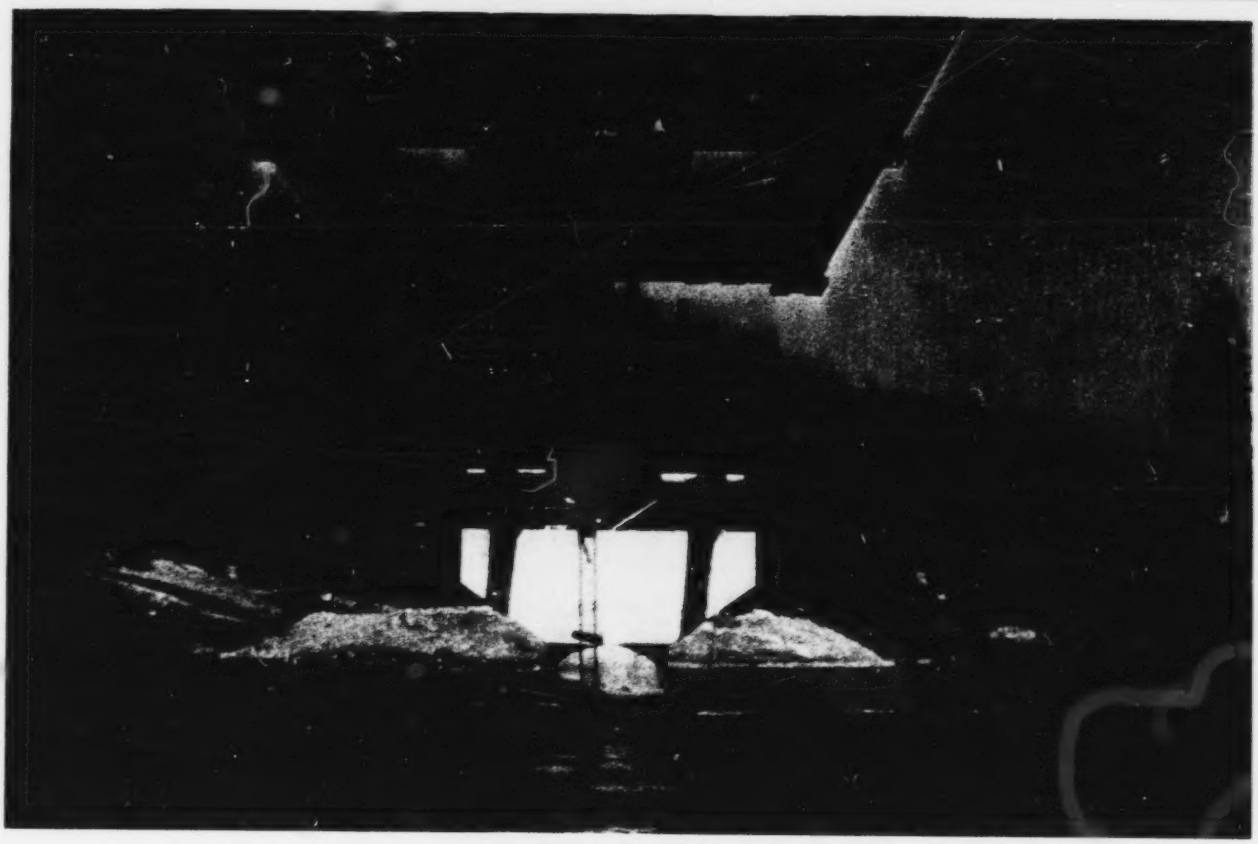
13. RELATED PARTY TRANSACTIONS

All of the outstanding shares of the railway are owned by the Government of the Province of British Columbia.

Long-term debt is guaranteed by the Province and the railway received a grant to assist with the related debt servicing charges as described in Note 8. The Ministry of Finance of the Province acts as fiscal agent in the administration of the long-term debt and the Superannuation Commission of the Province administers the railway pension plan. Fees are charged for both of these services. The majority of sinking fund assets comprise securities issued or guaranteed by the Province and include the securities acquired during 1982 at a discount as described in Note 1. The railway received grants during the year for rehabilitation projects and operating losses incurred on the Fort Nelson Extension. The railway also received grants for rehabilitation of the passenger car fleet and to partially cover the losses on the passenger operation, both as described in Note 12. No charge for property taxes on land used for railway purposes is made by the Province. Financing for the construction of the Tumbler Ridge branch line is being arranged by the Province as described in Note 4. All other transactions between the railway and the Province are at terms no more or less favourable than those with unrelated parties.



BRITISH COLUMBIA RAILWAY
1982 ANNUAL REPORT 1982



FINANCE

is being raised by means of additional debt, however, with the undertaking of the provincial government that at the first opportunity the debt will be retired using the proceeds of equity subscriptions in the company by the province. Until such subscriptions are completed, the province has undertaken to assist in the debt service charges related to the outstanding debt.

In recent years, the company's Finance division has kept pace with important business developments. Standards of work performance have been improved throughout the five major departments of the division and financial planning activities have been extended to a participatory budget process involving all railway managers.

Cash management techniques have been improved to ensure that the company receives optimum benefit from the funds under its administration. All major capital and operating projects are subject to financial analysis to determine their underlying business viability and operating methods and procedures have been streamlined wherever necessary to support growing information requirements. Both efficiency and productivity measurement techniques have been introduced to administrative systems necessary to support the waybilling process, collection of customer accounts, payment of supplier invoices and distribution of company payrolls. The company's Internal Audit department has received special attention to ensure that existing and proposed systems are carefully monitored.

The division's Data Processing department has moved from developing its initial operational systems in the early 1970s to an extensive data processing function involving virtually every aspect of company business.

With the support of the company's communications facilities, on-line, real-time computing service is available to all stations from North Vancouver to Fort Nelson, B.C. Computer systems have been developed for all significant business applications including materials handling; payroll and personnel; operational control; word-processing; construction; waybill handling and receivable and disbursement processing.

COAL TRANSPORTATION

The development of British Columbia's northeastern coalfield is the largest single undertaking in the history of the province. More than $2.6 billion is being invested over a three-year period, more than $500 million of which is to finance construction of B.C. Rail's new Tumbler Ridge branch line.

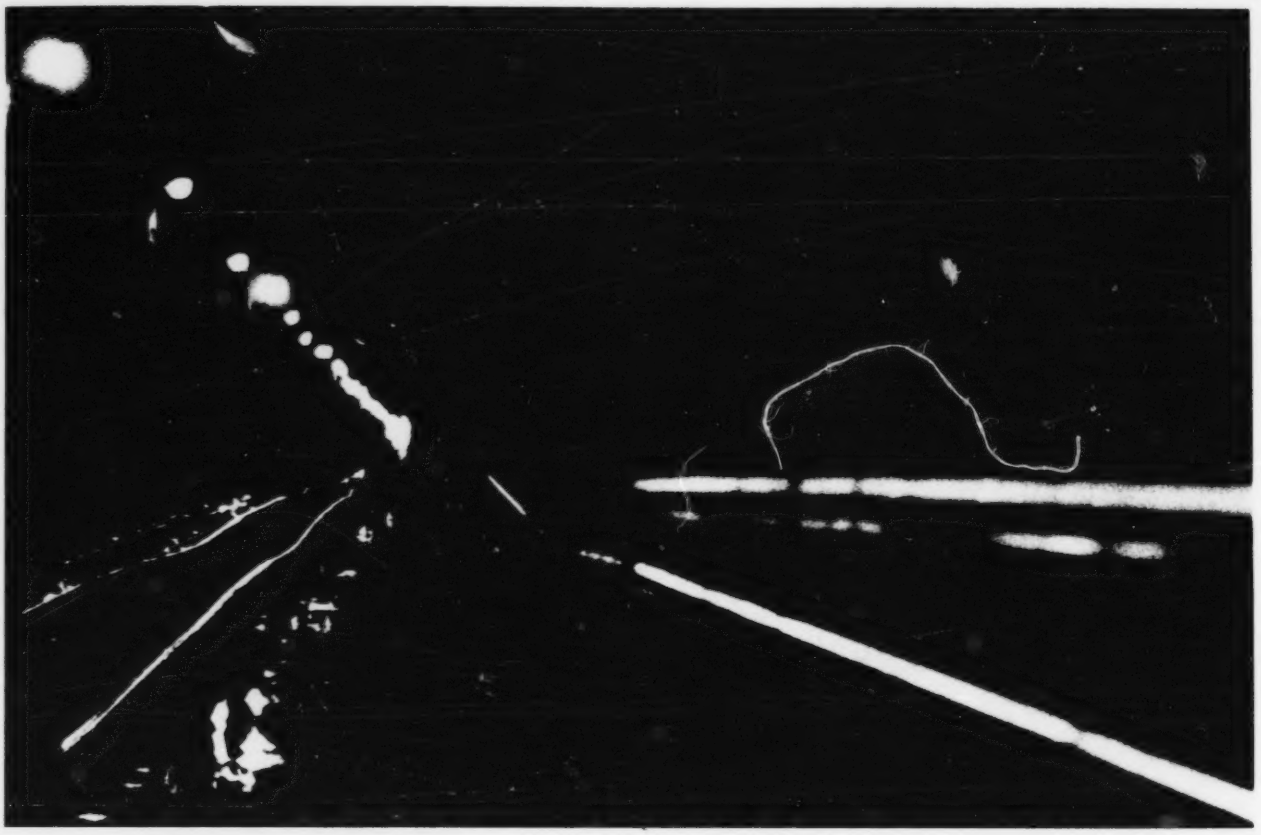
The 80-mile (129 km) line, through difficult, mountainous terrain, will link the coalfields with the railway's mainline at Anzac, B.C., 72 miles (116 km) northeast of Prince George. In conjunction with the Canadian National Railway, the 98-car, 13,000-ton unit trains will be hauled to a new, purpose-built deep-sea terminal under construction at Prince Rupert, B.C., en route to the steel mills of Japan.

The first coal sales contracts were announced in March, 1981, by the two mining corporations and the two levels of government involved.

Under the terms of the contracts, delivery was to commence in December, 1983 and in the very short time available to meet that commitment, B.C. Rail was required to engineer, design and construct a complete branch line. The line includes two major tunnels through the Rocky Mountains; two minor tunnels; loop tracks at the mine sites; seven major and four lesser bridges. Simultaneously, it was necessary for the railway to plan the upgrading of its existing mainline between Prince George and Anzac, to accommodate the heavy unit trains.

At the end of 1982, the new line was on schedule and within budget. Approximately 75 per cent of grade work was complete; all major bridgework was in place; the 5.6-mile (9 km) Table tunnel had advanced by 13,166 feet (4,013 m) and the 3.79-mile (6 km) Wolverine tunnel by 11,358 feet (3,462 m).

Electrification of the Tumbler Ridge branch line will place B.C. Rail in the forefront of international railway technology. Only two other railways in the world — an ore-carrying railway in South Africa and a coal line in Arizona — operate under a 50 kilovolt power supply. This advanced technology reduces the number of power substations necessary by more than half, a



COAL TRANSPORTATION

major consideration in deciding to electrify.

Aside from conservation of approximately two million gallons of high-grade diesel fuel annually, electric locomotive maintenance costs are approximately 65 per cent less than those of conventional diesel-electric units. The seven, 6,000 hp units on order from General Motors' Diesel Division in London, Ontario, will provide a more efficient, cleaner and quieter operation than would have been possible using conventional diesel engines. The life of an electric locomotive is approximately double that of a diesel-electric unit.

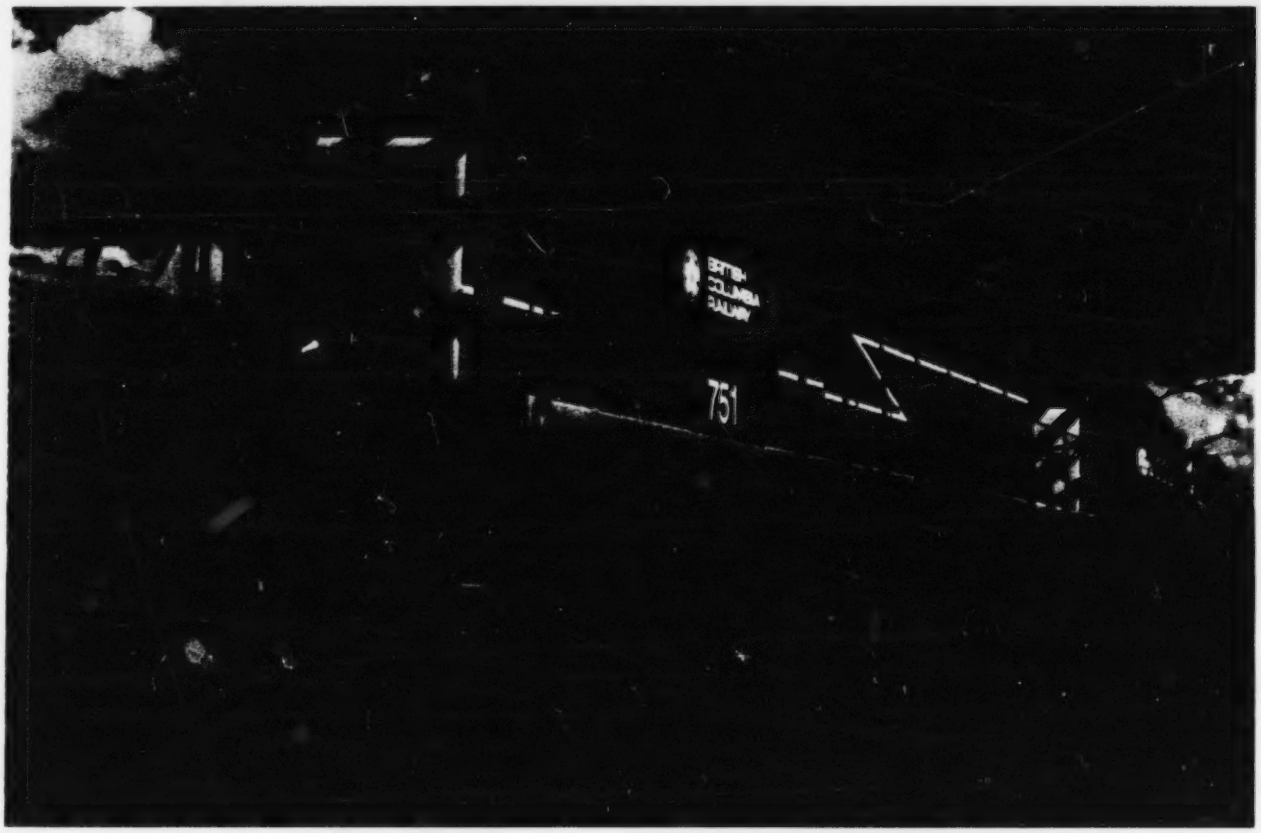
In addition, high tunnel ventilation costs, which would have been necessary for a diesel train operation, were avoided as a result of the decision to electrify. Fifty kilovolt technology, developed by Sweden's ASEA corporation, is acknowledged to be the most advanced in the world.

The unit trains are permanent train sets, equipped with rotary couplers for dumping, without uncoupling, at the Ridley Island (Prince Rupert) terminal. A nine-train, 75-hour cycle is planned between Tumbler Ridge and Prince Rupert and the first coal shipments are scheduled to move in December, 1983.

Current contracts call for up to 10 million tons of metallurgical coal to be shipped annually from the coalfields to Japan, which will more than double B.C. Rail's total annual freight movements and at the same time, lessen its heavy dependence on the forest industry. Over the next 15 to 20 years, there is potential for coal shipments to rise to as much as 30 million tons per annum.

As well as opening up a hitherto remote part of the province, it has been estimated that the North East Coal Development will directly and indirectly result in the creation of as many as 10,000 permanent new jobs in Canada, and approximately 46,000 man-years of construction work.

The success of this huge undertaking will depend upon a modern, reliable and efficient transportation system. Along with its partner in this project, B.C. Rail is providing the very best that technology has to offer.



MOTIVE POWER

B.C. Rail — then the Pacific Great Eastern Railway — became the first all-diesel railway in North America in the early nineteen-fifties.

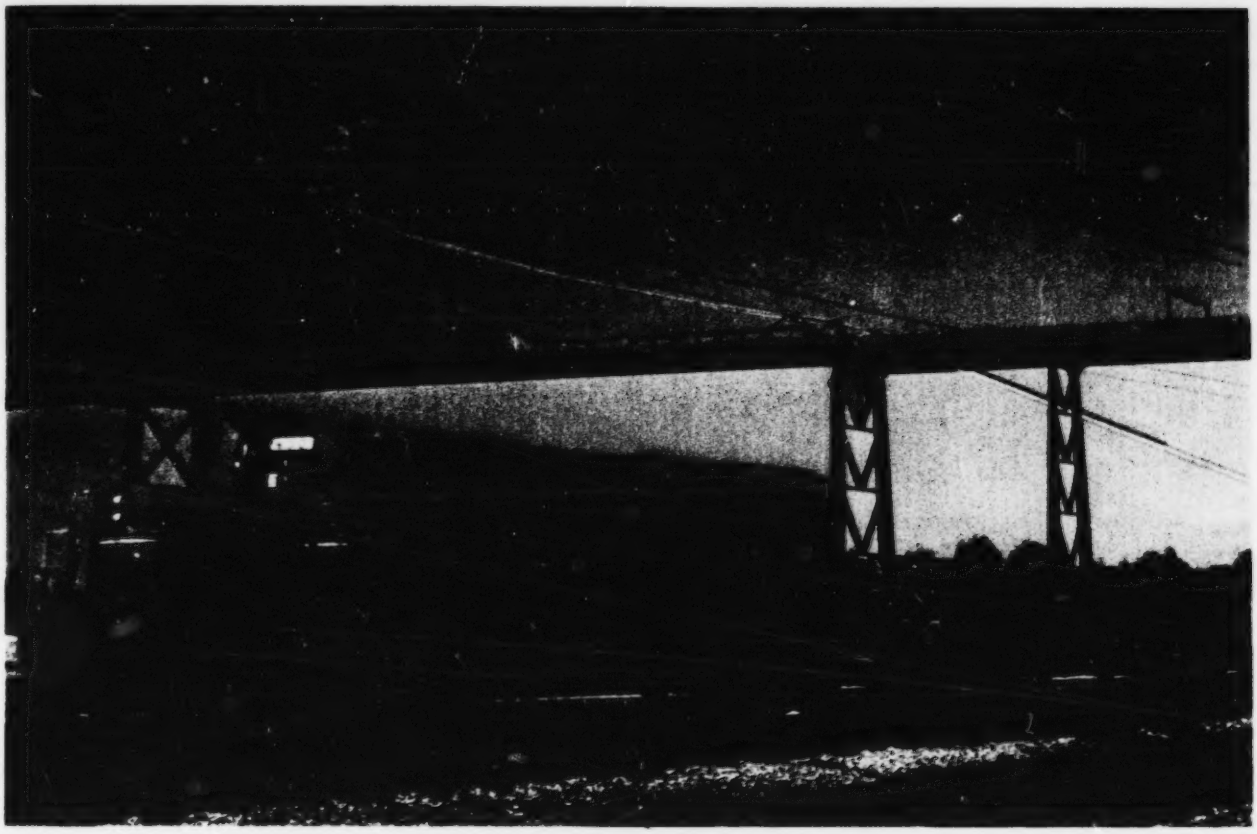
With the opening of its new Tumbler Ridge branch line in December, 1983, it will become Canada's first freight railway to be electrified and only the third in the world to use a 50 kilovolt (kV) power supply system.

As attractive an alternative as electric power is to B.C. Rail, however, diesel-electric locomotives continue to provide the bulk of Canadian railways' motive power. The great distances between generating stations, transmission lines and other carriers' mainlines make the prospect of wide-scale electrification in this country unlikely. The nation's present rail system was largely developed by diesel-electric locomotives. While there are excellent possibilities for incremental electrification of B.C. Rail's mainline in the years to come, it seems likely that Canada's other railways will be powered for the foreseeable future by diesel-electric units.

From 1970 to 1973, the company introduced remote control locomotives (RCL) for mid-train operation. Among other advantages, RCLs provide better air supply for braking and, because they are radio-controlled, emergency braking response is faster. In addition, the mid-train 'robots' significantly reduce draft-gear stress and in-train forces on front-end locomotives and throughout the train.

Between 1972 and 1982, sixty-three diesel locomotives were added to the railway's motive power fleet, including 12 new, 3,000 hp General Motors' SD40-2 diesel-electrics delivered in 1980. In preparation for operation of the electrified Tumbler Ridge branch line in December, 1983, seven 6,000 hp electric engines are to be delivered by the same manufacturer in the fall of that year. The new line will use a 50 kV power supply, one of very few railways in the world to do so.

During 1981, the railway developed and built a 'slug', which is best described as a switching engine auxiliary. The slug is a modified ALCO, 1,600 hp locomotive with cab and motor removed. Using only its below-deck electrics, the vehicle doubles the pulling



MOTIVE POWER

power of the attached switching-engine, at half the normal speed. Slugs are economical to operate, maintenance costs are low and because the slug has no diesel motor, 'idling' fuel burn is eliminated. Two additional slugs are to be built in 1983.

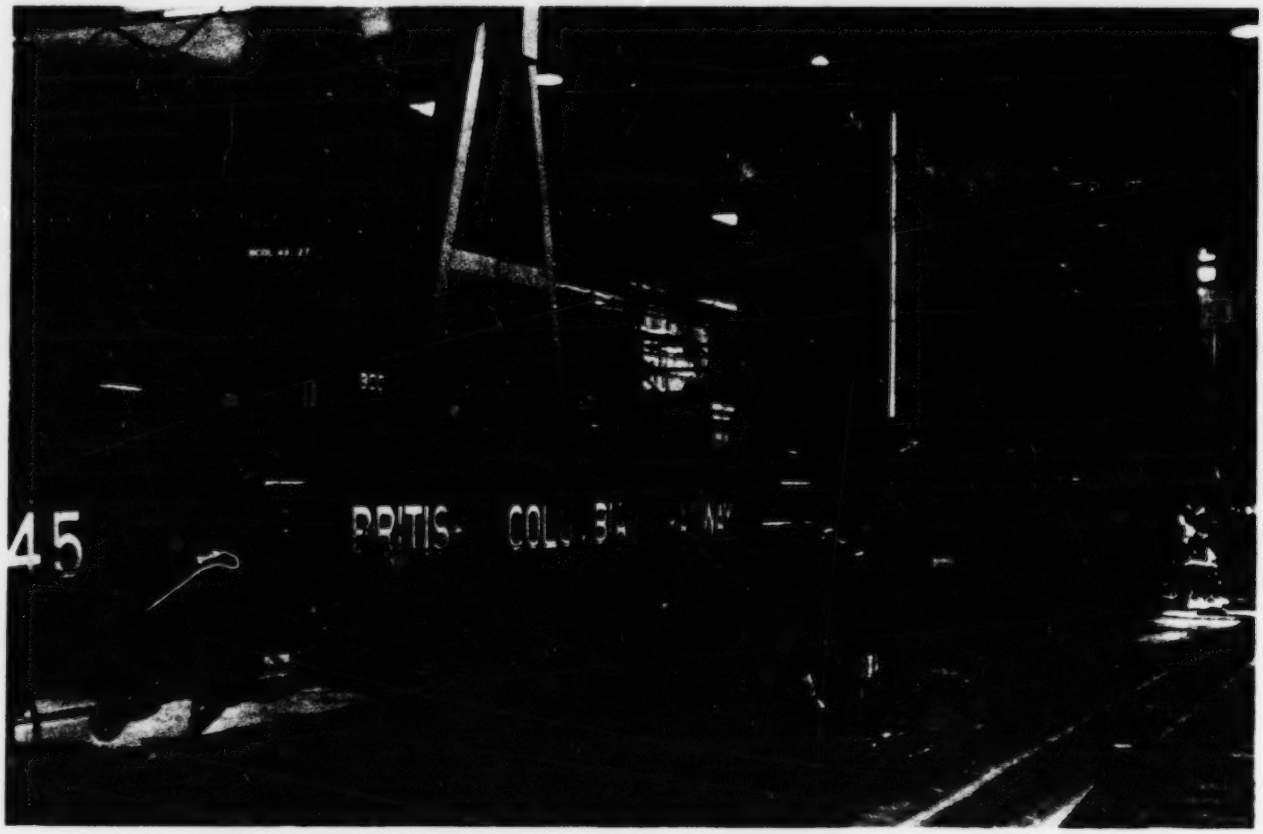
The railway today operates a fleet of 126 diesel-electric locomotives and six Budd rail diesel cars (RDCs) used in its passenger service between North Vancouver and Prince George. When the Tumbler Ridge branch line opens, the fleet will be augmented by the seven electric locomotives currently being manufactured by General Motors' Diesel Division in London, Ontario.

Since the price of petroleum fuel began escalating in the mid 1970s, B.C. Rail has been a leader in the continuing search for better fuel efficiency. It was a pioneer in the use of radio control of mid-train locomotives, a system which provides greater versatility in controlling trains over specific grades and route contours. With radio control, mid-train operations can be more precisely co-ordinated with the eight throttle positions in the head-end locomotive to provide improved overall efficiency and ease of operation.

The railway makes good use of simulator training which, among other things, on mock-up B.C. Rail routes, teaches enginemen to operate trains at optimum fuel efficiency. The device is a valuable aid in encouraging fuel conservation.

In January, 1982, B.C. Rail began using the fuel additive FE6, intended to reduce the exhaust of carbon deposits and cut back on forest fire risk in B.C.'s timbered regions. The additive had an attractive side benefit, however. It was found that as well as mitigating fire hazards, it also provided a 1.5 to 2 percent improvement in fuel consumption — more than enough to compensate for the additive's cost.

In the continuing search for improved fuel efficiency, another source of energy conservation was the adoption of diesel-electric locomotives equipped to produce alternating current instead of direct current. These are more efficient generators of horsepower.



ROLLING STOCK

As an originating carrier, B.C. Rail operates a fleet of nearly 10,000 railcars, 6,870 of which have been acquired during the past 10 years. Prior to the opening of the Tumbler Ridge line, 9 sets of 98-car unit coal trains will be added as a result of an agreement between B.C. Rail and CN Rail. The unit trains will be hauled from Tumbler Ridge to Prince George by B.C. Rail and from Prince George to Ridley Island Terminals, Prince Rupert, by CN Rail.

B.C. Rail's general fleet includes freight, box, flat, woodchip, hopper, tank and refrigerator cars, as well as cars specially-built for the railway's intermodal (piggyback) services. The size of the rolling stock fleet is disproportionate to the overall size of the railway as the majority of the traffic originating in B.C. is destined for U.S. and eastern Canadian markets. At any given time, as much as half of the railway's fleet may be off-line — much of it rented to other carriers and contributing as much as 15 percent of general revenues.

A sharp imbalance in north-south traffic, since the majority of B.C. Rail's revenue loads originate in northern B.C., calls for a precise and efficient system of car distribution to ensure that the right cars are in the right place at the right time. To help overcome the industry-wide problem of damaged cars, the railway maintains an audio-visual educational program, aimed at shippers and railway employees. The program is effective and has resulted in a marked reduction in shifting loads and car damage caused by careless handling.

The remarkable growth of B.C. Railway in the 1972—1982 decade is best illustrated by the substantial increase in the total fleet of rolling stock in that period. The years of greatest growth in freight car acquisitions were 1973 and 1980 but all were undertaken in anticipation of the steady growth which lies ahead, particularly as coal joins forest products and minerals as major sources of revenue. Relative to its size, the railway has a huge fleet because most of its business originates within its system and customers must be served with cars destined for markets mostly outside B.C.

MAINTENANCE

The most visible effects of B.C. Rail's reorganization and redevelopment are to be seen in its physical plant. A continuous program of redevelopment and renewal began in the early 1970s and in every sense, the railway has been brought up to first class operating standards. Today, it compares favorably with any rail system in North America.

The transformation was a quiet one. Between 1972 and 1982, an annual average of $10 million was invested in capital improvements and from its southern base in North Vancouver, B.C. to its northern terminus in Fort Nelson, the railway has been almost completely rebuilt.

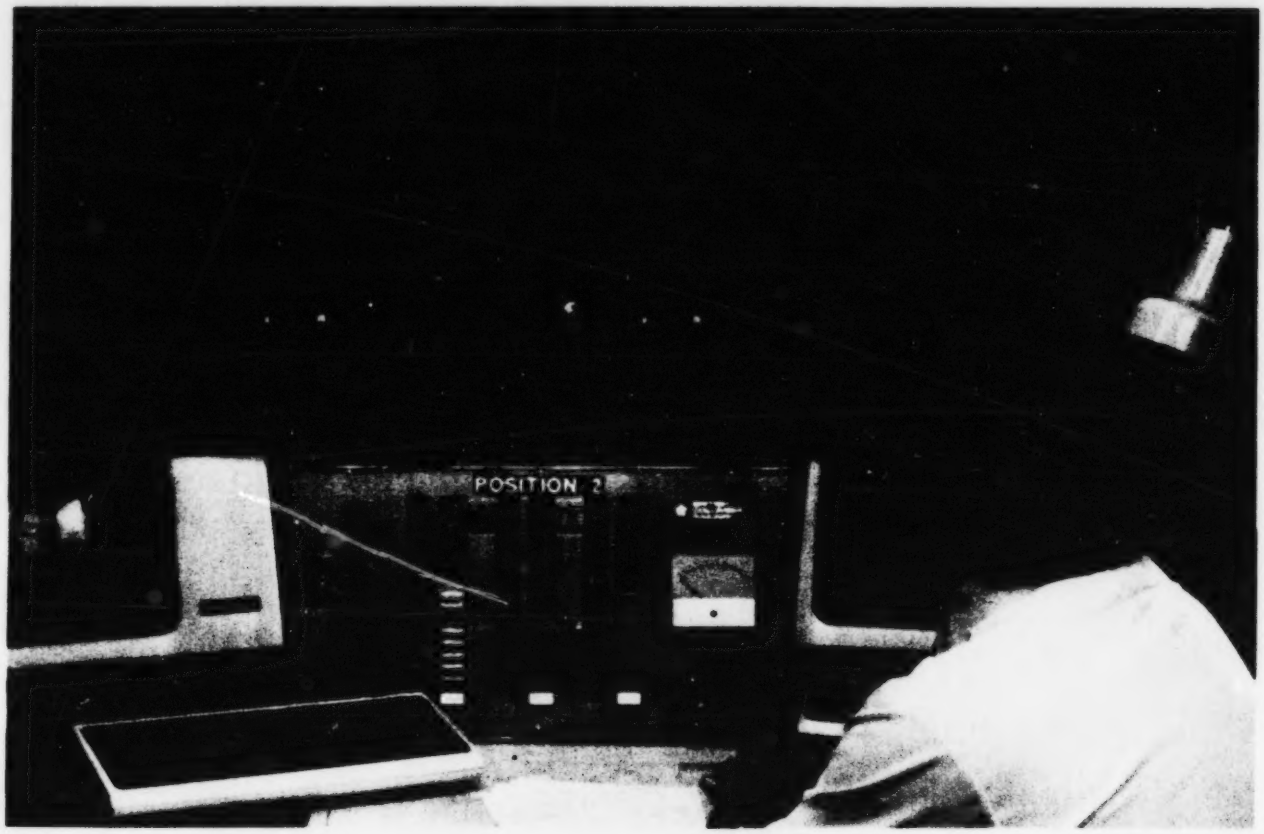
Throughout the railway's 1,260 miles (2,017 km) of mainline, deteriorating, untreated ties were replaced with high-quality creosoted ties. Spacing density was increased from 2,800 to 3,168 per mile.

During the last 10 years, 41 new prestressed concrete ballast deck bridges have been built and eight bridges have been replaced by fills. These structures replaced the aging trestle crossings that previously characterized the line. In 1973, a new 4,568-feet (1392 metre) tunnel was bored at Horseshoe Bay, West Vancouver.

The mainline, formerly a mixture of 60, 70, 85 and 100-pound rail, was replaced by 100 and 115-pound rail and on curves of six degrees or more, chrome rail was installed. Chrome rail is more resistant to the wear caused by the long, heavy trains the railway routinely operates.

Pit run gravel, which for many years formed much of the railway's mainline roadbed, was supplanted virtually throughout the system by crushed rock as part of the railway's continuing grade stabilization program. Where stabilization of existing grade was impractical, track was diverted and rebuilt to the same exacting standard.

In summary, B.C. Rail is in excellent condition. The intense program of modernization during the past 10 years, has earned it a reputation as a safe, reliable and competitive operator in the resource-shipping community — a reputation it will jealously preserve during the new era of resource development in its areas of operation.



LIC SYSTEM

B.C. Rail is now field testing a unique new traffic control system known as Location, Identification and Control (LIC). The system is a radio-controlled, computer-assisted method of directing and monitoring rail traffic.

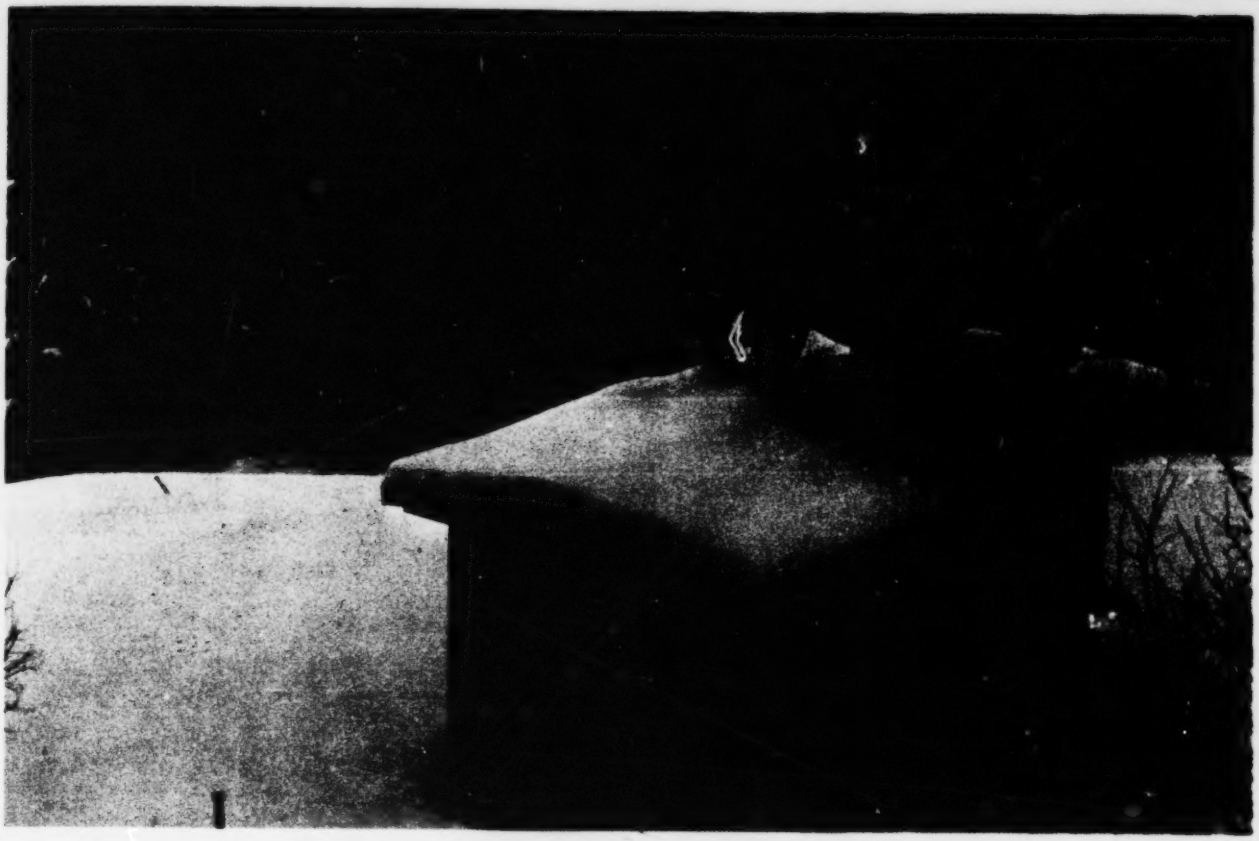
Some $3.6 million has been invested by governments and B.C. Rail during development of the system by Glenayre Electronics Ltd. It is being tested in the Squamish sub-division over 156 miles (251 kilometres) of track. Thirty-one locomotives and five self-propelled diesel cars now have visual display units (VDUs) which will show enginemen their train speed and location plus dispatcher orders.

Unlike many other railways, B.C. Rail is equipped with microwave radio and six existing stations are being utilized in the new system. B.C. Rail was the first North American railway to be equipped throughout with a microwave communications network. For LIC, 122 'transponders' were laid between the rails to signal the passage of trains to a computer in the dispatcher's office in North Vancouver. Here location and identity of trains will be continuously monitored.

Voice contact between dispatcher and enginemen will continue where necessary but up to three operating instructions at a time can be transmitted by the dispatcher to VDUs in locomotive cabs. Cabooses are equipped with radio transmitters, which will automatically advise train dispatch when trains have cleared switchpoints at sidings. Should the system fail, or should an 'unsafe' order be issued, alarms will sound and voice radio will be used as a backup system of control.

The LIC system contains built-in safeguards against failure and it is considered a major contributor to operating safety. The transponders operate without a power source and can be sealed against the weather.

A major advantage of LIC is its relatively low cost. To implement the developed LIC system will amount to $23,000 per mile, compared with $140,000 per mile for the already-developed CTC system. The LIC system has captured the attention of railways around the world and its progress is being closely watched. It is safer, cheaper and more efficient than conventional methods.



FUTURE

While the last few years have been years of improvement and development, the next decade promises to be one of consolidation and application of the skills acquired, along with the effective use of the first class physical assets and managerial expertise upon which the railway is now firmly established.

Profitability will continue to be an important goal in corporate strategy. Within the confines of its dual role as an instrument of provincial development and a commercial Crown corporation, the railway will strengthen its efforts to attain self-sufficiency and remain a valuable provincial asset. Like any other corporation, the railway's ability to grow will be controlled by the economic conditions of the day. Nevertheless, the company will continue to seek areas of diversification within its own field of expertise, as a means of lessening its dependence upon its present, relatively narrow revenue base. In that respect, the railway's involvement in the transportation of B.C.'s northeastern coal is a positive step forward. In the immediate future, the continuing development of the company's intermodal services product and exploitation of commercial opportunities for marketing communications facilities will combine to broaden the base still further.

In summary, the B.C. Rail of 10 years hence promises to be an efficient and administratively sound enterprise. Tomorrow's railway will be even more widely-regarded as a leader in international railway technology and as an enlightened employer of people. Its revenue base will have broadened to the point where its well-being no longer is bound exclusively to the fortunes of a single industry. At the same time, however, the railway will continue to provide the level of reliable, efficient and competitively-priced service that the provincial forest industry requires and expects.

B.C. Rail is in prime condition and it is in an excellent position to take full and immediate advantage of improved economic conditions when they occur. That this is so is largely the result of the past 10 years of renewal and progress.

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POOR

QUALITY

ORIGINAL